U.S. DEPARTMENT OF AGRICULTURE'S IMPLEMENTATION OF THE APRIL 1, 1985, REDUCTION IN THE NATIONAL SUPPORT PRICE FOR MILK

HEARING

BEFORE THE

SUBCOMMITTEE ON LIVESTOCK, DAIRY, AND POULTRY

OF THE

COMMITTEE ON AGRICULTURE
HOUSE OF REPRESENTATIVES

NINETY-NINTH CONGRESS

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CONTENTS

Page

Coelho, Hon. Tony, a Representative in Congress from the State of California, opening statement presented by Hon. Harold L. Volkmer, acting chairman .. 1
Gunderson, Hon. Steve, a Representative in Congress from the State of Wisconsin, opening statement ... 4
Jeffords, Hon. James M., a Representative in Congress from the State of Vermont, opening statement ... 2
Kastenmeier, Hon. Robert W., a Representative in Congress from the State of Wisconsin, prepared statement ... 7

WITNESSES

Anderson, Robert F., executive director, National Cheese Institute and American Butter Institute ... 41
  Prepared statement ... 96
Beren, David A., economist and director, milk procurement, Southland Corp ... 56
  Prepared statement ... 150
Bjornson, Neal R., assistant to the general manager, Associated Milk Producers, Inc ... 44
  Prepared statement ... 107
Christ, Paul, vice president, planning and dairy analysis, Land O'Lakes, Inc 51
  Prepared statement ... 133
Cropp, Robert A., professor and agricultural marketing specialist, extension, University of Wisconsin-Platteville ... 38
  Prepared statement ... 91
Eichstadt, James, director, communications, Farmers Union Milk Marketing Cooperative ... 53
  Prepared statement ... 142
Fraher, James, economist, Inter-State Milk Producers Cooperative ... 52
  Prepared statement ... 123
Goldberg, Richard A., Deputy Under Secretary, International Affairs and Commodity Programs, U.S. Department of Agriculture ... 8
  Prepared statement ... 60
  Final Regulatory Impact Analysis ... 69
Hamilton, Hal, dairy farmer, Community Farm Alliance of Kentucky ... 55
  Prepared statement ... 149
Saunders, Tom, dairy farmer, Prairie Farm, WI ... 55
  Prepared statement ... 148
Tillison, James E., executive director, Wisconsin Cheese Makers Association.... 45
  Prepared statement ... 116
Townsend, Thomas, vice president, Mid-America Dairymen, Inc ... 50
  Prepared statement ... 129

SUBMITTED MATERIAL

O'Connell, Richard T., president, Chocolate Manufacturers Association of the U.S.A., statement ... 155
Randall, Donald A., executive vice president-general counsel, National Independent Dairy Foods Association, statement ... 157
Tipton, E. Linwood, executive vice president, Milk Industry Foundation and International Association of Ice Cream Manufacturers, statement ... 161
Williams, Robert J., executive director, Trade Association of Proprietary Plants, statement ... 166

U.S. DEPARTMENT OF AGRICULTURE'S IMPLEMENTATION OF THE APRIL 1, 1985, REDUCTION IN THE NATIONAL SUPPORT PRICE FOR MILK

TUESDAY, MAY 21, 1985

House of Representatives,
Subcommittee on Livestock, Dairy, and Poultry,
Committee on Agriculture,
Washington, DC.

The subcommittee met, pursuant to notice, at 1:25 p.m., in room 1300, Longworth House Office Building, Hon. Tony Coelho (chairman of the subcommittee) presiding.

Present: Representatives Volkmer, Olin, Penny, Stenholm, Daschle, Bedell, English, Gunderson, Lewis, and Smith.

Staff present: Cristobal P. Aldrete, special counsel; John E. Hogan, minority counsel; Peggy L. Pecore, clerk; Kim Schnoor, Courtney Pastrick, Jeffrey Weiss, Bernard Brenner, Stephen R. Kerr, and Carol Ann Dubard.

Mr. Volkmer [acting chairman]. The Subcommittee on Livestock, Dairy, and Poultry will come to order.

OPENING STATEMENT OF HON. TONY COELHO, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF CALIFORNIA, PRESENTED BY HON. HAROLD L. VOLKMER, ACTING CHAIRMAN

Mr. Volkmer. The subcommittee is meeting today to receive testimony from a wide range of witnesses in our effort to determine just what the effects of the 50 cents per hundredweight dairy support price cut implemented on April 1, 1985, by the Secretary of Agriculture have been.

There have been indications from the dairy industry, manufacturers of dairy products, and congressional representatives that the net effect of this apparent 50 cents support price cut may have been much greater than the 50 cents reduction that was anticipated by USDA. We will attempt today to determine just what that cut has meant in terms of the actual dollar and cents impact on the industry, as well as how that cut impacts the financial difficulties that dairymen face as they struggle to run their operations. It is also important that we respond to the concerns of the manufacturers of dairy products who are directly impacted by the Dairy Program.

The strain of financial obligations of dairy producers today are evident and only further emphasize the need to assure that the intentions of the law are carried out and are not short or over extended. The Farm Production Expenditure Survey, compiled by USDA, indicates that most outstanding farm debt is owed by farmers in the highly leveraged and very highly leveraged categories. Statistics published by the USDA show that 36.9 percent of all dairy farms are in the highly leveraged category and 26.4 percent of dairy farmers are in the very highly leveraged category. This means that of over a quarter of all dairy farms are functioning with only 30 percent equity in their operations. Since liquidity is essential to the producer who does not have the ability to borrow, lower returns due to an excessive price reduction can surely add to these dairy farmers financial difficulties.

This subcommittee has the responsibility of reporting out legislation that will meet the budget guidelines set by the House of Representatives as well as to provide an adequate supply of milk and dairy products to the American people. However, we need to also learn from the current law and take into account the needs of our dairymen and how the implementation of the current law impacts the dairy manufacturing industry. We hope this hearing will provide us with the necessary information upon which to make the decisions that will serve the needs of all concerned, as well as assure that the intent of Congress was carried out by the Department of Agriculture.

I would like to welcome our first witness, the Deputy Under Secretary for International Affairs and Commodity Programs, Mr. Richard Goldberg, who is accompanied by Mr. Charles Shaw.

Mr. Secretary, I would like to ask that your statement be made a part of the record, and you may either review it or summarize it, however you so desire, but I would appreciate it if you could hold your testimony to approximately 15 minutes. You may proceed.

Mr. GUNDERSON. Mr. Chairman?

Mr. VOLKMER. Yes.

Mr. GUNDERSON. Mr. Chairman, would you mind, before we go on to that, if I could at least ask unanimous consent that opening statements may be made a part of the record by the members of the subcommittee.

Mr. VOLKMER. Yes, you may do so. Without objection, it is so ordered.

Mr. GUNDERSON. Thank you.

Mr. VOLKMER. If you have an opening statement you would like to make at this time, you may proceed.

Mr. GUNDERSON. If you want to get on with the witnesses, I will just make it part of the record at this point.

[The opening statements of Mr. Jeffords, Mr. Gunderson, and Mr. Kastenmeier follow:]

OPENING STATEMENT OF HON. JAMES M. JEFFORDS, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF VERMONT

Mr. Chairman, at the field hearings that the subcommittee held in Wisconsin and Vermont last month, we heard some disturbing testimony that suggested that the April 1 support price reduction was actually greater than the 50¢/cwt. that the 1983 Dairy and Tobacco Act authorized. The manner in which the Department adjusted purchase prices for butter, cheese and nonfat dried milk makes it difficult to determine just how much the support price was reduced. I do not say this as a criticism. I believe that we must allow the Secretary the discretion that the law gives him to adjust purchase prices as he sees fit. Those changes in purchase prices, however, must result in the change in the farm support price that Congress authorizes—no more, no less. I hope that we can resolve this question today.

The other issue to which I hope the witnesses will address themselves is the timing of the July price reduction. Odds are that the Secretary will excercise his authority to reduce the support price to $11/cwt. at that time. We have had some suggestions that deferring this change until October 1, when market prices will presumably be above the support price, would reduce some of the problems that price reductions unavoidably spawn. Thank you, Mr. Chairman.

STEVE GUNDERSON
3d District, Wisconsin

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OPENING STATEMENT
CONGRESSMAN STEVE GUNDERSON
LIVESTOCK, DAIRY & POULTRY SUBCOMMITTEE HEARING
MAY 21, 1985

MR. CHAIRMAN:

Ever since the Secretary announced reductions in the CCC purchase prices for dairy products on April 1, my office has literally been inundated with inquiries and complaints about the inequities of those cuts.

The vast majority of those contacts allege that the reductions will result in an overall drop in the support price for milk in excess of the $.50/hundred-weight authorized by Congress in 1983 if, on April 1, projected government purchases of surplus dairy products for the upcoming year exceeded 6 billion pounds (milk equivalent).

If those allegations are correct, USDA has, at a minimum, abused their statutory authority to make alterations in the purchase prices for dairy products. At a maximum, their action was a blatant attempt to discourage the purchase of dairy products by the CCC. In either case, dairy farmers will face a greater reduction in the price they receive for their milk than that authorized by law.

There seems to be two primary reasons for this disparity. First, USDA lowered the CCC purchase price for cheese by a greater proportion than the prices of butter and powdered milk.

The basis for this action is an assumed value for whey solids-not-fat of approximately one cent per pound of cheese which, in the past, has never entered into the calculation of the purchase price for cheese.

Our preliminary analysis of this change indicates that it is inappropriate because: 1) most cheese plants do not have whey drying facilities or access to such facilities and, thus, left-over whey is an economic cost to their operation, not an economic benefit; and 2) the "utilization rate" (i.e., the rate of human consumption) of 70 percent assumed by USDA is much too high--at least in the Midwest where much of our country's cheese is produced.

Second, USDA has increased the "price spread" between barrel cheese and block cheese from 3 cents per pound to 4.25 cents per pound.

Again, our analysis indicates that this change is improper because: 1) it is premised on "average" market price which was badly skewed by an unusually high six-week increase in that price differential; and 2) for the first time ever, USDA is not incorporating an offset in its barrel cheese calculation for the non-reusable fiber barrels in which CCC requires barrel cheese it purchases to be delivered. In the past, that offset has been about one cent per pound of cheese ($5 per barrel).

Accordingly, Mr. Chairman, information provided to my office suggests that producers who market their milk with barrel cheese plants--which are found primarily in the Midwest--will be subject to a reduction in the price they receive for their milk in excess of the $.50/hundredweight authorized by law as of April 1.

I, therefore, commend the Chairman for holding this special oversight hearing into whether or not USDA acted improperly in making its April 1 changes in the CCC purchase prices for dairy products and thank him for this opportunity to enter these opening remarks into the record at this time.

Statement of Testimony

by

ROBERT W. KASTENMEIER
Member of Congress

Mr. Chairman, members of the Subcommittee, I want to thank you for moving so quickly to hold these hearings into the surprisingly large decreases in purchase prices which Secretary Block announced would be implemented in order to accomplish the April 1st fifty cent cut in the support price for milk.

As I indicated to the Chairman in my letter of May 1, the announced purchase price cuts are clearly far in excess of the level of cuts which could historically be expected to accomplish a fifty cent cut in the support price. In actuality, it would appear that the announced cuts would effect a reduction in the support price of some seventy cents or more.

Secretary Block announced that the CCC purchase price for barrel cheese was being lowered 7.25 cents per pound while the price for block cheese was being lowered by 6 cents per pound. Those figures represent a dramatic increase over the 4.75 cent cut that was used in December, 1983, to accomplish the first fifty cent drop in the support price.

I might add that it is curious that the Secretary had decided to increase the spread between barrel and block cheese prices in making the announcement of these cuts. Traditionally, the spread between barrel and block cheese has been three cents. I would like to hear the rationale for increasing that spread by 1.25 cents.

It is clear to most people that this dramatic increase in the size of cuts in the CCC purchase prices is going to result in a higher cut in the support price. It has been indicated by the Department that the larger cut reflects a revision in the manufacturer's make allowance to increase the value of whey in calculating cheese manufacturing returns. That sounds fine in theory, but few cheese manufacturers realize any returns from whey sales and, in fact, most cheesemakers actually realize a cost for handling their whey.

The task of this subcommittee today will be to try to make some sense out of the figures and rationale provided by the Secretary. To me it would appear as though the Secretary has exceeded his authority by decreasing the support price for milk by over seventy cents per hundredweight when he was only authorized to reduce the support price by fifty cents per hundredweight. I would like to urge the Subcommittee to consider revoking the Secretary's authority for an additional support price reduction on July 1, 1985. In light of the excessive nature of the April 1 cut, and anticipating the passage of legislation as part of the 1985 Farm Bill which will significantly alter the dairy program, the July 1 cut could be deemed to be not only unnecessary, but likely damaging to the preservation of our dairy industry.

Mr. VOLKMER. We will now hear from Mr. Goldberg.

STATEMENT OF RICHARD A. GOLDBERG, DEPUTY UNDER SECRETARY, INTERNATIONAL AFFAIRS AND COMMODITY PROGRAMS, U.S. DEPARTMENT OF AGRICULTURE, ACCOMPANIED BY CHARLES SHAW, AGRICULTURAL STABILIZATION AND CONSERVATION SERVICE

Mr. GOLDBERG. Thank you, Mr. Chairman. I normally would summarize, Mr. Chairman, but the request is of a fairly technical nature, so I am going to try to review the technicalities.

Mr. Chairman and members of the subcommittee, I am happy to be here today to talk about the reduction of April 1 and also the effect on purchases which is the request of the chairman.

At the outset, let me indicate that the April 1 reduction and the administrative actions which implemented the reduction are all set forth in the Final Regulatory Impact Analysis dated March 26. I request, Mr. Chairman, that a copy of the analysis be incorporated in the record with this statement.

[The Final Regulatory Impact Analysis appears at the conclusion of the hearing.]

Mr. GOLDBERG. The national support price for milk was reduced 50 cents per hundredweight on April 1, as we know, in accordance with the provisions of section 201(d) of the Act of 1949 as added by the Dairy and Tobacco Adjustment Act of 1983. I welcome the opportunity to briefly address some of the administrative actions taken by the Secretary and to simultaneously clear up any misunderstanding or misinformation which has spread through the dairy industry as a result.

At the outset, I would like to emphasize that the April 1 administrative actions taken were based on the best information available at the time the decisions were made. We believe that, as a package, they were in the best interests of not only the Commodity Credit Corporation but the dairy industry and the taxpayers as well. We further believe that these actions were clearly consistent with the objectives of supporting the price of milk to farmers in accordance with legislative mandates, managing CCC inventories effectively and efficiently, and achieving cost savings without adversely affecting the price support objectives.

In announcing the decision on March 29, 1985, Secretary Block emphasized that the package of actions was an effort to reduce incentives for the dairy industry to sell dairy products to CCC as a primary market outlet. Since much debate in connection with the farm legislation which is currently under consideration will focus on surplus dairy products, Commodity Credit wants to ensure that Government policy is not encouraging the excessive sales of such products to CCC. The role of CCC and the legislative mandate is to provide a price support to farmers that will ensure an adequate supply of milk. There should be no question of the U.S. dairy industry's capacity to meet these requirements.

There are some other important considerations that underlie the administrative decisions which took place on the 1st of April. It must be remembered that the dairy support program is national in scope and, out of necessity, must be based on averages. Also, the industry has the capacity to shift quickly in response to economic factors from producing cheese to producing butter/nonfat dry milk, and vice versa from the available milk supply. Therefore, it is critical to maintain a balance between the support purchase prices for those products purchased by CCC.

Now, let's get to the changes that were effective on April 1. The first item on the agenda is manufacturing allowances.

Manufacturing allowances, or make allowances, are designed to reflect the annual average costs for manufacturing cheese and butter/nonfat dry milk. Manufacturing allowances were continued at the current levels of $1.22 per hundredweight of milk for butter/nonfat dry milk and $1.37 per hundredweight of milk for cheese. Conclusive data were not available upon which to base any change in these allowances. Moreover, any increase in the allowances would have directly offset the effect of the lower support price.

The most reliable indication of the adequacy of the allowances has been the difference between the average U.S. manufacturing milk price and the support price when CCC is buying reasonable, but not excessive, quantities of all three dairy products.

During the first 7 months, October 1984 to April 1985, of this marketing year, the average price received by farmers was exactly equal to the average support price during that period, a period during which CCC purchased over 6 billion pounds of milk equivalent of dairy products. This fact suggests that CCC's current manufacturing allowances are set at reasonable levels.

We did not increase the manufacturing allowance, and contrary to reports published in the dairy industry, we did not lower it.

CCC sales policy: The Commodity Credit dairy product sales policy of setting sell-back prices at 110 percent of support purchase price was retained. It was recognized that processors would have on hand dairy products that were made from milk produced prior to April 1 of the reduction period. Therefore, products which were produced before April 1 and graded and offered to CCC by April 15 were purchased by us at the older higher support price.

Concern has been expressed by the industry relating to inventory value losses due to the drop in support price. While this concern is understood, an inventory value reduction will necessarily follow a price support reduction. And, it should be noted, the impact can be converse. For example, in years past when support prices were increasing, sometimes twice a year, the industry was the recipient of an inventory value gain.

Price differential between block and barrel cheese: The price differential which CCC pays between block and barrel cheese was increased from 3 cents per pound to 4.25 cents per pound. This change more accurately reflects current and historical market value differentials and could encourage some shift from purchases of barrel cheese to block cheese. That has not occurred, Mr. Chairman, and I will get to that later.

Some have complained about this change and have used barrel cheese as an example to suggest that CCC actually lowered the support price not by 50 cents per hundredweight but by 60 to 70 cents per hundredweight. Some have stated that small barrel cheese plants have been disadvantaged, and that may be true. However, it is not the mandate of CCC to provide a sole market for or a profit for any particular plant or group of plants. Furthermore, to select the price impact on a single product purchased by CCC as a measure of the overall net effect of a reduction in the price support level is not proper since the industry can adjust to any misalignment in price.

Single nationwide purchase price established for butter: Prior to April 1, Commodity Credit announced only one purchase price for butter at New York City. A price at any other location was a calculated adjustment based on published freight rates.

Last year, the Interstate Commerce Commission exempted rail transportation of dairy products from regulation which eliminated the requirement to publish the freight rates. In the absence of published freight rates, the single price system will be easier to administer than either the previous system or establishing a three-price regional system as suggested by some. The CCC purchase price is now the same for all regions, and that practice is identical to the practice for the purchase programs for cheese and nonfat dry milk.

Purchase prices for butter and nonfat dry milk: The reduction in the support price for milk used in making butter and nonfat dry milk was allocated totally to nonfat dry milk.

In recent years, purchases of nonfat dry milk have far exceeded, relative to their portions present in milk, purchases of butter. CCC has been purchasing 60 to 70 percent of total nonfat dry milk produced in the United States.

Last fall, when markets tightened, butter prices increased to CCC sell-back levels while nonfat dry milk prices remained at support levels, an indication that purchase prices for those products were misaligned.

Putting all the decrease on NDM might lead to a net increase in commercial use of nonfat milk solids and a substantial reduction in CCC costs as compared to allocating the decrease equally between nonfat dry milk and butter which was the case in the past.

Allowance for value of whey solids nonfat established in calculating cheese purchase prices: A net value of 2.5 cents per pound of whey solids was established based upon a 15 cent dried whey average price minus an estimated 12.5 cents per pound processing cost and an estimated 70-percent utilization rate. The resulting amount, about 1 cent per pound of cheese, was deducted from the purchase price which would otherwise have been established for cheese.

In fiscal year 1984, the weekly market price for whey powder for Central States production area averaged 15.3 cents per pound. During the first 31 weeks of 1985, it has averaged 19.6 cents per pound.

Moisture levels for cheese: The maximum acceptable levels of 38.5 percent for block and 36.5 for barrel were retained. Also, no additional premiums will be paid for moisture content below 34 percent.

This does not mean that CCC will not buy cheese that is below 34 percent. It means that CCC will pay no additional premium. All barrel cheese is purchased at a premium over the announced price as is much of the lock cheese. This change should have little, if any, economic impact on cheese plants.

For CCC purposes, moisture levels in the ranges specified are consistent with proper inventory management. Of the barrel cheese in inventory, about one-tenth of that purchased since July 1, 1984, was below 34-percent moisture, so it is minimal.

Mr. Chairman, your letter specifically requested that I address the effect of the price cut on purchases. It is premature to measure any long-term effect. However, as noted previously, CCC purchased at the old, higher price those products produced before April 1 if graded and offered prior to April 15.

Since April 1, CCC has purchased the following quantities of products compared with the same time—and I am not going to read the table, Mr. Chairman, except to show you that the relationship between butter and nonfat dry milk and the relationship between block and barrel cheese has narrowed in the first 2 weeks in May. Therefore, we feel our program is working effectively.

In conclusion, Mr. Chairman and members of the subcommittee, I believe that the actions taken by Secretary Block on April 1 were sound, responsible actions for the good of both the American taxpayer and the U.S. dairy industry. We have had relatively few complaints about those actions. In fact, favorable comments, both publicly and privately, which we have received substantiate our decision. The Department believes the decisions were fair, equitable, and accurately reflect the statutory requirements mandated by the Congress in the 1983 Dairy and Tobacco Adjustment Act.

I thank you, Mr. Chairman, and I will be glad to answer any questions.

[The prepared statement of Mr. Goldberg appears at the conclusion of the hearing.]

Mr. **Volkmer**. Thank you, Mr. Goldberg.

At this time, I will recognize the gentleman from Wisconsin.

Mr. **Gunderson**. Thank you, Mr. Chairman.

Mr. Secretary, thank you for your statement and for giving us the perspective of the Department views on this issue. I have to tell you that my fears were confirmed on page 2 of the statement when you said that Secretary Block emphasized that the package of actions was an effort to reduce incentives for the dairy industry to sell dairy products to CCC as the primary market outlet. I thought the intent of the price support system was to establish a price for the farmer, not to determine incentives or disincentives to sell to the Government.

I think I must tell you that, at a minimum, I think there may be an abuse of discretion here, and at a maximum, probably there is a blatant attempt by the Department of Agriculture to try to prevent certain purchases from USDA. I would like to begin by asking if you don't agree——

Mr. **Coelho**. Would the gentleman yield?

Mr. **Gunderson**. I would be happy to yield.

Mr. **Coelho**. If we can, with unanimous consent, I would like to make sure that the statement of our colleague, Congressman Bob Kastenmeier, is inserted in the record prior to the presentation by the current witness. Without objection, it will be done.

Mr. **Gunderson**. I would like to begin by asking if you don't agree that the process by which you calculated this 50-cent price deduction is, at a minimum, inconsistent with past practices.

Mr. GOLDBERG. I don't think so, Congressman. Our calculations indicated, that even at the current purchase level, we are still going to purchase 9 billion pounds.

Mr. GUNDERSON. That is not the question, Mr. Goldberg. I asked if the process by which you have calculated this reduction is not different in the considerations from everything from whey to barrel versus block cheese, to the moisture content, to the New York versus Chicago butter price. At a minimum, isn't the process by which you determined this price cut inconsistent with the historical tradition that USDA has used to calculate the price in the past?

Mr. GOLDBERG. To be perfectly honest with you, Congressman, I am told that the formulation that we used was what we have done in the past in part, but in part the formulation was changed. If you would like me to respond for the record at a later time, I would be glad to, because it is a technical question that I really can't answer.

[The information follows:]

The enclosed documents indicate the same method has been used in the past in calculating whey values and the corresponding adjustment in cheese purchase prices.

Page 3 of the press release USDA 756-77 outlines the decision by CCC to purchase barrel cheese.

Calculation of Whey Value other than fat for 1974-75 Marketing Year

Market price for dry whey	14 cents per lb.
Processing and transportation costs	7 cents per lb.
Return to cheese plants	7 cents per lb.
Yield per 100 pounds of whole milk used to make cheese	5.5 pounds
Value per 100 pounds of milk	$.385
Portion of U.S. production of liquid whey which is processed	40 percent
Weighted U.S. average whey value per 100 pounds	.154

ASCS/CMO/3-11-74

Calculation of CCC purchase prices for dairy products with support at 80% of parity as of Jan. 1, 1975 ($7.24 per hundredweight.)

Revised

Item	Apr.-Dec. 1974	Effective Jan. 4, 1975
Support price for manufacturing milk	1/ 6.57	7.24
Average milkfat test	3.67	
Yields per 100 pounds of milk (pounds)		
Butter	4.48	
Nonfat dry milk	8.13	
Cheese	10.1	
Butter purchase price at New York	.6200	.695
Butter purchase price at Chicago	2/ .6057	2/ .6807
Butter-Nonfat dry milk price calculation		
Return to butter-powder plants per cwt.	6.57	7.24
Margin between price of manuf. milk and the market value of butter and n.f.d.m. made from 100 pounds of milk	.72	.72
Market value of butter (Chicago) and n.f.d.m. (U.S. average) made from 100 pounds of milk	7.29	7.96
Value of butter per 100 pounds of milk (Chicago)	2.72	3.05
Value of n.f.d.m.:		
Per 100 pounds	4.57	4.91
Per pound	.5621	.6039
(adjusted)	3/ .566	4/ .606
Cheese price calculation		
Return to cheese plants per cwt.	6.57	7.24
Spread between price of manuf. milk and the market value of cheese and whey fat per 100 pounds of milk	.87	.87
Market value of cheese and whey fat per 100 pounds of milk	7.44	8.11
Value of .25 pound of whey fat 5/	.15	.17
Value of other whey solids	.15	.15
Value of cheese:		
Per 100 pounds of milk	7.14	7.79
Per pound: calculated	.7069	.7715
rounded	.7075	.7725

1/ Estimated 80 percent of parity as of April 1, 1974.

2/ Prices based on actual freight rates in effect April 1, 1974. The price of .608 previously used for April-December was based on estimated freight rates.

3/ Includes adjustment as follows: .2 cent for the extra cost of 50 pound bags, and .2 cent to compensate for the 2-cent reduction of the CCC purchase price of butter in the West. (Butter production in the West is about 20 percent of U.S. production; 20 percent of the 2 cent reduction is .4 cent per pound of butter nationally. This is equivalent to 1.79 cents per hundredweight, or .22 cents per pound of nonfat dry milk.)

4/ Includes .2 cent extra to compensate for the 2 cent reduction of the CCC butter purchase price in the West.

5/ Butter purchase price at Chicago times .25.

ASCS/CMO/Dairy/1-2-75

Calculation of CCC purchase prices for dairy products with support at $7.24 per hundredweight

Item	Effective Jan. 4, 1975	Effective Apr. 1, 1975
Support price for manufacturing milk	7.24	7.24
Average milkfat test	3.67	3.67
Yield per 100 pounds of milk (pounds)		
Butter	4.48	4.48
Nonfat dry milk	8.13	8.13
Cheese	10.1	10.1
Butter purchase price at New York	.695	.7075
Butter purchase price at Chicago	.6807	.6919
Butter-Nonfat dry milk price calculation		
Return to butter-powder plants per cwt.	7.24	7.24
Margin between price of manuf. milk and the market value of butter and n.f.d.m. made from 100 pounds of milk	.72	1/ .77
Market value of butter (Chicago) and n.f.d.m. (U.S. average) made from 100 pounds of milk	7.96	8.01
Value of butter per 100 pounds of milk (Chicago)	3.05	3.10
Value of n.f.d.m.		
Per 100 pounds	4.91	4.91
Per pound	.6039	.6039
(adjusted)	2/.605	.605
Cheese price calculation		
Return to cheese plants per cwt.	7.24	7.24
Spread between price of manuf. milk and the market value of cheese and whey fat per 100 pounds of milk	.87	1/ .92
Market value of cheese and whey fat per 100 pounds of milk	8.11	8.16
Value of .25 pound of whey fat 3/	.17	.17
Value of other whey solids	.15	4/ --
Value of cheese:		
Per 100 pounds of milk	7.79	7.99
Per pound: calculated	.7715	.7911
rounded	.7725	.7[illegible]

1/ Includes estimated increase in the last two years in processing costs which more than offset increased efficiencies of manufacturing plants.

2/ Includes .2 cent extra to compensate for the 2 cent reduction of the CCC butter purchase price in the West.

3/ Butter purchase price at Chicago times .25.

4/ Zero value reflects recent drop in market prices of whey products to a level which barely covers processing costs for such products.

ASCS/CAO/Dairy/4-1-75

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NEWS
U.S. DEPARTMENT OF AGRICULTURE

USDA TO INCREASE MILK PRICE SUPPORT:

WASHINGTON, March 22--Secretary of Agriculture Bob Bergland today announced that the support price for manufacturing milk for the 1977-78 marketing year will be $9.00 per hundredweight. This is estimated to be 83 percent of parity on April 1 and compares to the present support of $8.26, which is now only 76 percent of parity.

Legislation requires that milk be supported at a level between 75 and 90 percent of parity to assure an adequate supply of milk, reflect changes in the cost of production and assure a level of farm income adequate to maintain productive capacity sufficient to meet anticipated future needs.

The announced increase in support will result in an estimated annual rise in cash receipts of about $3,000 for a producer with a 40-cow herd. The increase is equivalent to an increase in the retail price of fluid milk of about one and one-half cents per quart.

There has been severe drought in important milk producing areas in the West and Mid-West. As a result, feed costs have risen significantly in the last several months. Hay and other roughages have been in very short supply, and producers have been forced to truck needed supplies from distant areas at greatly increased costs. In some localities, the cost of hay has more than doubled.

Moreover, the market prices for milk have dropped 70 cents per hundredweight, nearly 8 percent, in the last six months.

As a result of the higher feed costs, and much lower milk prices, the milk-feed price ratio, an important measure of the profitability of producing milk, has declined substantially in recent months. The milk-feed price ratio (pounds of feed equal in value to a pound of milk) was 1.49 in February, down

- more -

from both November's 1.65 and last February's 1.66. The difference between the price of 100 pounds of milk and 100 pounds of concentrate ration was $3.14 in February, down from $3.91 in November and $3.90 a year ago.

The Secretary said that today's announced increase would accomplish the objectives of legislation and assure that milk prices received by farmers will keep pace with increases in the prices farmers must pay for feed and other costs of production, including the rising cost of energy, another important item in the cost of producing milk. Today's increase in the support price will help producers pay these higher costs and continue in dairying.

The support price announced today will be reviewed again in six months to determine if further adjustments are needed to carry out the legislative objectives.

The support level is achieved through offers by the Commodity Credit Corporation (CCC) to purchase carlots of butter, American-type cheese and nonfat dry milk at announced prices. The purchase prices, listed in the table on page 4, are designed to result in a national annual average price paid to farmers at least equal to the announced support price.

The price advantage for cheese under the support program will be eliminated. CCC purchase prices in effect since April 1, 1976, have enabled cheese manufacturers to pay dairy farmers 30 cents per hundredweight more than butter-nonfat dry milk manufacturers. This provision was established last year to avoid increasing the purchase price for nonfat dry milk and to minimize the increase in the purchase price for butter. The provision is no longer advisable since cheese production and stocks have risen sharply.

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In order to better enable barrel cheese manufacturers to pay producers the support price for their milk, CCC will purchase barrel cheese in fiber barrels for an indefinite period at 95 cents per pound--3 cents less than the price for block cheese. A decision on whether to continue buying barrel cheese on a permanent basis will be made at a later date, based on CCC's experience with storage and processing, and on whether there is a continuing need for such purchases. Barrel cheese, which is used mainly to make American process cheese, represents 60 percent of the American-type cheese produced in the U.S.

Prices of barrel cheese have been severely depressed in the past several months and have remained depressed even though CCC bought large quantities of process cheese. CCC will continue to purchase Cheddar cheese in 40-pound blocks at the announced price and will continue to buy process cheese, as needed, on a competitive bid basis.

The sale by CCC of high-moisture and old nonfat dry milk on competitive bids is being temporarily discontinued. CCC inventories of such nonfat dry milk have been reduced substantially through past sales and donation program dispositions, and it is not necessary to continue sales at this time.

In order to encourage the industry to store its own dairy products for use in the short production season of the fall and winter, the CCC sales prices of dairy products for unrestricted use will be increased from 105 to 110 percent of the current CCC purchase prices. In addition to providing more incentive for the industry to store products, the higher sell-back prices will cover increased carrying costs.

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Support Purchase Prices for Dairy Products

	Produced before April 1, 1977	Produced on or after April 1, 1977
	- - - - Dollars	per pound - - - -
Butter, U.S. Grade A or higher		
New York City and Jersey City, Newark and Secaucus, New Jersey 1/	.9275	1.0275
Nonfat dry milk (spray) U.S. Extra Grade (but not more than 3.5 percent moisture)		
50-pound bags: Unfortified	.6240	.6800
Fortified (Vitamins A&D)	.6340	.6950
Cheddar Cheese, standard moisture basis		
40-pound blocks, U.S. Grade A or higher	.9250	.9800
500 pounds in fiber barrels, U.S. Extra Grade	--	.9500

1/ The price of butter located at any other point outside these cities will be the price at New York minus 80 percent of the lowest published domestic railroad through freight rate for frozen butter per pound gross weight for a 60,000 pound carlot from such other point to New York City (in effect on April 1 of each marketing year). However, no price at any location shall be less than the purchase price at New York City minus 3 cents per pound. The support purchase at Chicago, for butter produced on or after April 1, 1977 is estimated to be $1.0071 per pound.

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Table 3: Calculation of CCC Purchase Prices for Dairy Products With Support at $9.43, effective April 1, 1978, and $9.87, effective October 1, 1978 8/

Item	Effective April 1 - Sept. 31, 1978	Effective October 1, 1978
Support price for manufacturing milk,$/cwt.	9.43	9.87
Average milkfat test, percent	3.67	3.67
Yields per 100 pounds of milk (pounds)		
Butter	4.48	4.48
Nonfat dry milk	8.13	8.13
Cheese	10.1	10.1
Butter-Nonfat dry milk price calculation		
Return to butter-powder plants, $/cwt.	9.43	9.87
CCC **margin** between price of manuf. milk and the **value** of butter and NDM made from **100** pounds of milk, $/cwt.	1.12	1.12
Value of butter (Chicago) and NDM (U.S. **average**) made from 100 pounds of milk, $/cwt.	10.55	10.99
Nonfat dry milk purchase price, $/lb.	.71	.7375
Value of NDM per 100 pounds of milk, $/cwt. 1/	5.77	6.00
Value of Butter:		
Dollars per 100 pounds of milk	4.78	4.99
Dollars per pound at Chicago (calculated) 2/	1.0670	1.1138
Butter purchase price at New York, $/lb.	1.0875	1.1350
Butter purchase price at Chicago, $/lb.	1.0671 3/	1.1130 4/
Cheese price calculation		
Return to cheese	9.43	9.87
Margin between price of manuf. milk and the **value** of cheese and whey per **100** pounds of milk, $/cwt.	1.27	1.27
Value of cheese and whey per **100** pounds of milk, $/cwt.	10.70	11.14
Value of .25 pound of whey fat, $ 5/	.27	.28
Value of other whey solids, $	- 6/	.15 7/
Value of cheese:		
Dollars per 100 pounds of milk	10.43	10.71
Dollars per pound (calculated) 8/	1.0327	1.0604
Cheese purchase price (rounded), $/lb.	1.0325	1.0600

1/ NDM price per pound times 8.13. (The increase in support split about equally between butter and nonfat dry milk.)

2/ Value of butter per hundred pounds of milk divided by 4.48. (Chicago butter price is representative of U.S. average price.)

3/ Price based on actual freight rate in effect on Oct. 1, 1977.

4/ Price based on estimated freight rate in effect on Oct. 1, 1978.

5/ Butter purchase price at Chicago times .25.

6/ Estimated zero net return on nonfat whey solids 4/1/78-9/31/78.

7/ Estimated that 80 percent of whole milk cheese whey solids other than fat will be processed at a 3.5¢ net return (13.5¢ dried whey average price minus 10¢ processing costs) per pound (5.5 lbs. whey solids not fat in 100 pounds of milk used to make cheese).

8/ Value of cheese per hundred pounds of milk divided by 10.1.

ASCS/PSD/Dairy/10-2-78

Calculation of CCC Purchase Prices for Dairy Products with Support
at $10.51 per cwt., effective April 1, 1979,
and $11.22 per cwt., effective October 1, 1979

Item	Effective April 1- September 31, 1979	Effective October 1, 1979
Support price for manufacturing milk, $/cwt. at 3.5% milkfat	10.51	11.22
Support price for manufacturing milk, $/cwt. at 3.67% milk	10.76	11.49
Average milkfat test, percent	3.67	3.67
Yields per 100 pounds of milk at average test (pounds)		
Butter	4.48	4.48
Nonfat Dry Milk	8.13	8.13
Cheese	10.1	10.1
Butter-Nonfat Dry Milk Calculation		
Return to butter-powder plants, $/cwt.	10.76	11.49
CCC margin between price of manuf. milk and the value of butter and NDM made from 100 pounds of milk, $/cwt.	1.12	[1]1.22
Value of butter (Chicago) and NDM (U.S. average) made from 100 pounds of milk, $/cwt.	11.88	12.71
Nonfat dry milk purchase price, $/lb.	.79	.84
Value of NDM per 100 pounds of milk, $/cwt. [2]	6.42	6.83
Value of Butter:		
Dollars per 100 pounds of milk	5.46	5.88
Dollars per pound at Chicago (calculated) [3]	1.2188	1.3125
Butter purchase price at New York, $/lb.	1.2400	1.3400
Butter purchase price at Chicago, $/lb.	[4]1.2180	[5]1.3133
Cheese Price Calculation		
Return to cheese	10.76	11.49
Margin between price of manuf. milk and the value of cheese and whey per 100 pounds of milk, $/cwt.	1.27	[1]1.37
Value of cheese and whey per 100 pounds of milk, $/cwt.	12.03	12.86
Value of whey:		
.25 pounds of fat, $ [5]	.30	.33
Other solids, $	[7].02	[8].00
Total, $	.32	.33
Value of cheese:		
Dollars per 100 pounds of milk	11.71	12.53
Dollars per pound (calculated) [9]	1.1594	1.2406
Cheese purchase price (rounded), $/lb.	1.1600	1.2400

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[1] 10-cent per hundredweight increase in manufacturing margin.

[2] NDM price per pound times 8.13. (The increase in support split about equally between butter and nonfat dry milk.)

[3] Value of butter per hundred pounds of milk divided by 4.48. (Chicago butter price is representative of U.S. average price.)

[4] Price based on actual freight rate in effect on Oct. 1, 1978.

[5] Price based on estimated freight rate in effect on Oct. 1, 1979.

[6] Butter purchase price at Chicago times .25.

[7] Estimated that 70 percent of whole milk cheese whey solids other than fat is processed at a 0.5¢ net return (10.5¢ dried whey average price minus 10¢ processing costs) per pound (5.5 lbs. whey solids-not-fat in 100 pounds of milk used to make cheese.)

[8] Estimated that 70 percent of whole milk cheese whey solids other than fat is processed at 0¢ net return (11¢ dried whey average price minus 11¢ processing costs) per pound.

[9] Value of cheese per hundred pounds of milk divided by 10.1.

ASCS/PSD/Dairy/10-2-79

Mr. GUNDERSON. Can you cite for us the authority you have under law to use broad discretion in making the determination of how you will or will not calculate the price?

Mr. GOLDBERG. No, sir, I cannot. I don't have the information.

Mr. GUNDERSON. Will you provide that for the record as well, the legal basis by which the USDA has decided to make this determination?

Mr. GOLDBERG. I would be happy to.

[The information follows:]

The legal basis utilized by the USDA was Section 201 of the Agricultural Act of 1949, and the CCC Charter Act which provides among other things for the protection of the assets of the Corporation.

Mr. GUNDERSON. Let's talk for a bit about this spread issue, if we can. You mentioned in your testimony that the old price spread between block and barrel cheese was 3 cents per pound, did you not?

Mr. GOLDBERG. I believe that is correct, yes.

Mr. GUNDERSON. And you also indicated that on April 1 you increased that spread to 4.25 cents per pound. Is that correct?

Mr. GOLDBERG. That is right.

Mr. GUNDERSON. What market and for what period did you look at to arrive at that spread?

Mr. GOLDBERG. That, Congressman, was an historical market price calculation.

Mr. GUNDERSON. I am not sure I totally agree that is what USDA used. It is my understanding that the time period you used, however, was different. You used the Green Bay exchange. Correct?

Mr. GOLDBERG. I think that is correct.

Mr. GUNDERSON. And you used a specific time period there. Is that not correct?

Mr. GOLDBERG. That is correct.

Mr. GUNDERSON. Do you know what that time period was?

Mr. GOLDBERG. No, I don't.

Mr. GUNDERSON. Mr. Shaw, do you know?

Mr. SHAW. Congressman, I am not sure I agree that a specific time period was delineated on this. We look at this historically over the last several years, and we work on annual averages.

Mr. GUNDERSON. I am not sure I agree with you. We have been told by USDA and others in the past that it was a specific time period used for that. My concern is that the time period used is different than the fact that 36 of the 52 weeks during the time the price spread on the Green Bay exchange was less than 4.25 cents per pound. So, you selected out of there a very small 12-week period to use and claim that is your historical base when, if you look at the last year, you can't defend that particular base.

Mr. GOLDBERG. I am told, Congressman, that we did not set a certain number of weeks nor did we intentionally try to pick a period. I am sure that in those calculations as well as the other calculations, we took as long a period of time as we possibly could in order to get the correct average.

Mr. GUNDERSON. Will you provide the committee with the specific timeframe you used for that calculation?

Mr. GOLDBERG. We would be happy to.

[The information follows:]

The attached table shows price differences between block cheese and barrel cheese specifically, the column labeled diff. under exchange for the past 5 years 1980-84 shows 5.03¢, 4.88¢, 4.21¢, 2.95¢ and 4.27¢, respectively, that average is 4.27 cents. This 5-year period was the time frame used. The difference using the assembly point prices during the same 5 years is even more pronounced.

Cheese Prices Barrels and Blocks

	Exchange			Assembly Points		
	bbls.	blocks	diff.	bbls.	blocks	diff.
1975	.8065	.8345	.0279	.8260	.8661	.0401
1976	.8798	.9217	.0419	.9084	.9630	.0546
1977	.8960	.9393	.0433	.9132	.9683	.0551
1978	1.0061	1.0411	.0350	1.0216	1.0708	.0492
1979	1.1287	1.1771	.0484	1.1543	1.2377	.0834
1980	1.2427	1.2930	.0503	1.2704	1.3304	.0600
1981	1.3083	1.3571	.0488	1.3394	1.3944	.0550
1982	1.3154	1.3575	.0421	1.3348	1.3827	.0479
1983	1.3230	1.3525	.0295	1.3381	1.3831	.0447
1984	1.2986	1.3413	.0427	1.3078	1.3796	.0718

Mr. GUNDERSON. Are you familiar with the fact that the CCC purchases barrel cheese only in nonreusable fiber barrels?

Mr. GOLDBERG. That is right.

Mr. GUNDERSON. Are you also aware of the fact that when a buyer other than the Government purchases barrel cheese through the Green Bay exchange in one of these special barrels he is charged extra for that?

Mr. GOLDBERG. That is correct.

Mr. GUNDERSON. Does your 4.25 cent per pound price spread account for this added cost of the barrel?

Mr. GOLDBERG. No, sir, it does not. I would like to remind the Congressman that this has been going on since 1977, and we feel that the startup period has been absorbed over the last 7 years and that the industry can now absorb the cost of going to the fiber barrel.

Mr. GUNDERSON. So, you are saying this is a change, then?

Mr. GOLDBERG. It is a change from what we went for 7 years with the figure that you are talking about.

Mr. GUNDERSON. My time is up, Mr. Chairman. I have some more questions.

Mr. COELHO. We will make an exception. We know you have to leave, and I want to make sure you can pursue your questions. You have an additional 3 minutes.

Mr. GUNDERSON. Thank you, Mr. Chairman.

Let's go on to the whey issue, if we can, Mr. Goldberg. It is my understanding from your testimony that a portion of the decrease in the purchase price for cheese that occurred resulted from a first-time assumption of a value of whey solids not fat. Is that correct?

Mr. GOLDBERG. That is correct.

Mr. GUNDERSON. And the value you assumed was 10 cents per 100 pounds or 1 cent per pound, 10 cents per 100 pounds of milk processed. Is that correct?

Mr. GOLDBERG. That is correct.

Mr. GUNDERSON. How was that 10-cent figure arrived at?

Mr. GOLDBERG. I am going to let Mr. Shaw take that, because he did the economic analysis.

Mr. GUNDERSON. Thank you. Go ahead.

Mr. SHAW. Congressman, on that one, whey has an economic value so that we estimate a value for the sale price of the whey. We estimated a cost for drying and converting the whey into that product. We utilized a 70-percent utilization rate as the proportion estimated to be further processed, and that worked out to 10 cents per hundredweight on milk which equates to about 1 penny per pound on cheese.

Mr. GUNDERSON. Isn't it a fact, however, Mr. Shaw, that very few cheese plants in the United States have facilities to dry whey and get a value for it?

Mr. SHAW. That may be true when you talk of individual plants. However, many cheesemakers have other ways of shipping whey to those who do dry it to utilizing it for other uses. The point is the whey as a byproduct has an economic value which the Department felt must be included in calculating the return to the cheesemakers.

Mr. GUNDERSON. If your incentive was to reduce purchases by the CCC, I can understand that, but I would remind you that only 31 of the 287 cheese plants in my State have whey-drying facilities and only 80 of the 678 cheese plants in the United States have any kind of a whey-drying facility. So, to suggest that this has an economic value rather than an economic hindrance, I think you would agree, begs the questions and, certainly, the law of averages, would you not?

Mr. SHAW. Well, I believe we would have to continue to assert that it has economic value as evidenced by the numbers in the testimony showing the value of the first 31 weeks of this year. I believe it was 19 cents per pound.

Mr. GUNDERSON. Of what, the whey?

Mr. SHAW. Of the whey.

Mr. GUNDERSON. By how many plants, sir?

Mr. SHAW. We don't deal with individual plants, Congressman. To do that would require us to go out and audit individual plants and their total operations which we don't believe would be in the interest of either the Department or the Government to do.

Mr. GUNDERSON. Can you indicate and tell this subcommittee that for the average cheese plant in this country whey has an economic value rather than an economic cost to deal with in the standards of their respective State departments of natural resources?

Mr. SHAW. On the average, for the U.S. cheesemaking industry, we estimate a value for the industry as a whole which is the way we operate the total price-support program, on averages. Some are above average, some are below, and some have costs, and some have receipts.

Mr. GUNDERSON. Well, I would suggest to you that when 250 of the 287 plants in my State do not have a whey-drying facility and when 600 of the 678 plants nationwide do not have a whey-drying facility to suggest that what you have calculated is average is what we call in this town and across the country new math.

Thank you, Mr. Chairman.

Mr. COELHO. Thank you, Mr. Gunderson. You have some interesting questions, interesting answers.

Mr. Penny.

Mr. PENNY. Mr. Goldberg, who in the Department made the determination that we were going to change our calculation on both whey and on the cheese price support?

Mr. GOLDBERG. Are you talking about barrel and block cheese?

Mr. PENNY. Yes; who made the decision that we were going to change our calculation both in terms of the value we apply to whey and to the price spread between barrel and block?

Mr. GOLDBERG. The analysis was done by ASCS. The decision was made by the Department at a high policy level.

Mr. PENNY. Was it that the analysts generated that recommendation from the bottom up or did somebody from the top on down say this is what we want you to do or find a way to do this?

Mr. GOLDBERG. Well, Congressman, we don't operate that way. The package of options was generated from the bottom up, as it always is.

Mr. PENNY. At someone's request?

Mr. **Goldberg**. No, sir, absolutely not. It is an administrative procedure, Congressman, and what we suggest is the best way to operate the program. The numbers that I have already given to the subcommittee and our analysis would indicate in the short period of time, and I emphasize it is a short period of time, would indicate we are going in the right direction. Certainly, if you look at the numbers on barrel and block cheese, you can see that we are on the right track.

Mr. **Penny**. Were there other options that were recommended from the analysts to people at the top of the Department?

Mr. **Goldberg**. Yes, Congressman; we looked at a number of other options, one of which was to continue what we have done in the past.

Mr. **Penny**. So, the analysts set forth alternatives and somebody made a decision that this was the alternative that you were going to pursue.

Mr. **Goldberg**. The impact statement was signed by the Secretary. So, eventually, those statements were made by the Department at a policy level, but the workup for it, in answer to your original question, was done from the bottom up.

Mr. **Penny**. Where, again, did you get the statistics on the value of whey? What was the source again?

Mr. **Goldberg**. The statistics for the value of whey?

Mr. **Penny**. What was your source of those statistics?

Mr. **Goldberg**. That, again, Congressman, was a market analysis of what whey products are worth. I should correct a statement I just made. The impact statement which differs from the policymaking statement was signed by myself, not the Secretary.

Mr. **Penny**. So, this proposal, in particular, has your fingerprints all over it.

Mr. **Goldberg**. I would say there are quite a few fingerprints all over it, Congressman. I am not going to disown it, if that is what you are suggesting.

Mr. **Penny**. In calculating that value for whey, do you maintain that is an industrywide average value?

Mr. **Goldberg**. That is correct.

Mr. **Penny**. You maintain that it is. Can you demonstrate that it is?

Mr. **Goldberg**. I can't do it for you at the hearing, Congressman.

Mr. **Penny**. It is somewhat disconcerting that somehow there is a value applied when the evidence is that in most plants it is a cost to that plant to have to handle the whey.

Mr. **Goldberg**. Well, Congressman, you can pick out a plant in Minnesota or——

Mr. **Penny**. No; we are picking out an awful lot of plants where they get no value out of the whey, and that is what I am saying. If you have evidence to prove that you took all of those plants where it is a net loss into account, and you still come up with a value for the whey, I would like to see those statistics. It amazes me that somehow you can come out with a net value for this whey when in most production facilities in this country, it results in a net loss for them to have to handle the whey.

Mr. **Goldberg**. Congressman, we do not have numbers of statistics on individual plants. That would require, as you can well imagine in your own State, quite an auditing procedure for us to accomplish.

Mr. PENNY. It is indicated that there is about a 70-percent utilization rate. That is a USDA assumption or a USDA statistic. Did you calculate in the loss or the net cost of the 30 percent that is not utilized in identifying the value for whey?

Mr. GOLDBERG. We did not figure the 30 percent in figuring our cost.

Mr. PENNY. I think I will let that answer stand on its own, Mr. Chairman. Time has run out.

Mr. COELHO. Mr. Bedell.

Mr. BEDELL. I hesitate to get into this because of my lack of expertise in this area, but when did your increased differential on cheese take effect?

Mr. GOLDBERG. April 1.

Mr. BEDELL. Was it effective April 1 or was it effective April 15 or when was it effective?

Mr. GOLDBERG. It was effective April 1, Congressman, for products produced after April 1. For products, as I mentioned earlier, that were produced prior to April 1 and graded, we bought those products at the previous support level.

Mr. BEDELL. I guess the only argument I have is short, but you made a big issue over the fact that you had seen quite a change from barrel to block cheese. I do not think your figures show that necessarily. I think it depends completely upon what you take. Certainly, from April 1 to May 15, it has gone the other direction very dramatically. From April 1, 1984, until this time, it has not changed. I am not here to make a big issue of it, but I think you have to document things a little better. If you are going to try to say that this clearly shows something, you had better have some figures that clearly show it.

You give me your arguments, and I will give you arguments right back from this table that can refute those just as completely, I think.

Mr. GOLDBERG. Congressman, our numbers will show that we are still buying a substantial amount of barrel cheese. We had hoped that we would pick up an increase in block as a result of the change, but that has not occurred. So, had we proceeded the way we did before, the situation would have been far worse because we would have had more of the same. So, it may be too soon to tell exactly how this thing will all wash out, but at the moment, at least, we are still buying substantial amounts of barrel cheese.

Mr. BEDELL. But you are buying less than you were on April 1, and you are buying much, much less in regard to block cheese. So, actually the proportion has switched more and more to barrel cheese compared to April 1. I don't think that is worth pursuing with a lot of the subcommittee's time. The only thing I would like to point out is that for this member, your statement of how clearly these figures document the progress you have made, I think, is certainly debatable to anybody, but I don't want to take any more of the subcommittee's time.

Mr. COELHO. Thank you, Mr. Bedell. I tend to agree with you. I think at this hearing all we are finding out is that there is a lot more information that we need to have. I don't think that the witnesses have documented the reasoning for the decisions that they have made. When you base a decision on freight rates just because ICC is no longer required to show those rates and even the industry has agreed to provide the information, the industry has agreed to provide the data that they need, and the USDA still does not use that, I think there are a lot of questions here that need to be pursued, and I intend to pursue them.

Mr. Volkmer.

Mr. VOLKMER. I am also concerned about both the questions of the gentleman from Wisconsin and the gentleman from Iowa. Maybe I should continue on with that of the gentleman from Iowa.

Was it the intent of the Agriculture Department in formulating the formula for determining the 50-cent reduction to make it so that the cheese manufacturers would convert from barrel to block? Was that one of the purposes?

Mr. GOLDBERG. In part, that is true. We tried to encourage more butter purchases the way we did it. But if you look at our numbers in cheese, block versus barrel, if you take the last 2 weeks in April and the first 2 weeks in May, there is not an appreciable difference which indicates, as I was explaining to Congressman Bedell, that they have not been disenfranchised. But if you look back a year——

Mr. VOLKMER. Excuse me, but that is in spite of what you tried to do.

Mr. GOLDBERG. Well, we are better than we were.

Mr. VOLKMER. Let me ask you why did you want that conversion to take place?

Mr. GOLDBERG. Because, Congressman, we had, if you look at our numbers back in mid-1984, if you look at the ratio between block and barrel, we were purchasing about four times more barrel cheese than we were block cheese. We felt that in doing what we did on April 1, we would begin to bring the thing together. If you look at the numbers, they have improved somewhat. But again, I must emphasize to the members of the committee that we are less than 60 days into the new program.

Mr. VOLKMER. And you are still hoping that there will be more block and less barrel?

Mr. GOLDBERG. Well, we are obviously going in that direction. In the first 2 weeks in May 1984, the block was 3.4. Block in 1985 was 6.4. If you look in the next column, the spread is a little better.

Mr. VOLKMER. Well, what is obvious to me, maybe you won't admit it, but you made the discrepancy in the formula as to the additional 1.25 cents in order to bring this about, did you not?

Mr. GOLDBERG. That is correct.

Mr. VOLKMER. Even though, realistically, it didn't exist and there is no real reason for it other than you no longer wanted barrel cheese; you wanted block cheese. You wanted more block and less barrel, so you made the discrepancy.

Mr. GOLDBERG. Well, I don't say that is a discrepancy, Congressman. The 1.25 cents was a part of it, but the market told us that in terms of what was happening that was what should be done.

Mr. VOLKMER. Also, it has been brought out by the gentleman from Wisconsin—perhaps I should ask this question with regard to the dry whey and the processors and the few numbers that have it.

Let's assume that none of the cheese manufacturers have processing facilities for the drying of the whey and they all had to dump it. Would you put in your formula that they could have the processors and therefore we are going to give them an additional 2.5 cent credit for being able to handle that even though they don't have it? Would you say that?

Mr. **GOLDBERG**. If that were the case, Congressman, we probably would not, no.

Mr. **VOLKMER**. So, just because a relatively few number have these facilities, you are saying that all the rest of them should have it, too, and just because they don't, we are still going to have them take credit for having it.

Mr. **GOLDBERG**. Congressman, we looked at the market value of whey products across the board and did not get down to individual plants and which did and did not have capability of doing it. Obviously, there is a strong market for whey and it is an added value product.

Mr. **VOLKMER**. Is that whey in liquid form from the processors of cheese or is that after it is dry?

Mr. **GOLDBERG**. I believe you can buy whey in either form.

Mr. **VOLKMER**. None of the cheese facilities dump the whey?

Mr. **GOLDBERG**. Some do, yes.

Mr. **VOLKMER**. It is a waste product, and it costs them to even do that.

Mr. **GOLDBERG**. Some do if they can't get rid of it. In my other life when I was in the feed business, we used to buy whey, both liquid and dry.

Mr. **VOLKMER**. But did you take into consideration the numbers that do not have the facilities for drying the whey?

Mr. **GOLDBERG**. We didn't, Congressman, because we have no way of knowing, plant by plant. We have no data on individual plants.

Mr. **VOLKMER**. We don't have that many plants in the United States that a quick survey couldn't tell you whether or not they have facilities, surely. I mean, there are 600 and some cheese plants?

Mr. **GOLDBERG**. Close to 700 plants, I believe.

Mr. **VOLKMER**. And a survey of 700 plants is not feasible for the USDA to determine whether or not they have facilities to process the whey? The gentleman from Wisconsin just mentioned the figures, approximately how many there are—I don't know—but he found out somehow.

Mr. **GOLDBERG**. I don't see how you would manage a program, Congressman, based on which plants can do what in any of these programs. The very best we can do and the most equitable way of doing it is to ascertain market prices and apply it across the board. If you go down to every dairy or any other processing plant in this country and allocate governmental assistance on the basis of what their capability on an individual basis is, that would be an impossible and a very inequitable situation for the Department. We would not be managing our inventories or our program very well.

Mr. **VOLKMER**. But if a vast majority of them do it one way while a numerical minority do it another way, you have taken the minority.

Mr. **Goldberg**. I don't know if we have or not, Congressman, because we, as I told you before, we have not made an inventory check.

Mr. **Volkmer**. I am just curious, in the event that we have another reduction July 1, are we going to look at the very same thing?

Mr. **Goldberg**. I don't know, Congressman. It is too soon to tell.

Mr. **Volkmer**. My last question, Mr. Chairman, is back in December 1983 when we had a reduction, I believe equivalent to around a $4.85 or $4.75 figure?

Mr. **Goldberg**. You mean on a price per pound of cheese?

Mr. **Volkmer**. Yes, reduction. Isn't that right?

Mr. **Goldberg**. That is about right. Mr. Shaw says that is correct.

Mr. **Volkmer**. And that is a lot less than what we had this time for the same 50 cents. The 50 cents hasn't changed, but now the amount, the reduction for the purchase price, has changed from around $6 and $7.25 from the $4.75 or $4.85. I am just wondering how that came about.

Mr. **Goldberg**. We recognize, Congressman, that this is a change from the way we calculated things in the recent past. On the other hand, I think when we took a more realistic approach as to what these values really are and we tried to apply them as equitably as we could across the whole industry.

Mr. **Volkmer**. Well, what it appears to me is that, Mr. Goldberg, your new formula actually ends up being, the result of it is, that it is more than a 50 cent reduction, as Congress proposed, to most of the dairy farmers are going to be selling milk on a manufactured basis.

Mr. **Goldberg**. Well, let me answer it this way, Congressman. I am sure that there are some plants, minor in numbers, that that would be correct, that the 50 or 60 cents or what you have heard. But I would maintain that across the board that would not be true.

Mr. **Volkmer**. You mean there are going to be some that are going to be less than 50 cents?

Mr. **Goldberg**. Not less.

Mr. **Volkmer**. Well, if there are not that are going to be less, some that are going to be more, the average isn't going to be 50 cents.

Mr. **Goldberg**. Well, the butter plant could be under 50 cents.

Mr. **Volkmer**. Thank you, Mr. Chairman.

Mr. **Coelho**. Thank you, Mr. Volkmer.

Mr. Goldberg, in making these changes, did the Department consider the possibility that when you implemented them on April 1 that they could or that they would go over 50 cents?

Mr. **Goldberg**. We recognized in all these calculations, Congressman, as in the past, that you will have an isolated situation where that can happen.

Mr. **Coelho**. Do you also know that under the law or do you agree that under the law if you implement a price cut that you cannot exceed 50 cents? Do you agree to that or do you not?

Mr. **Goldberg**. That is true, and I maintain that we have not.

Mr. **Coelho**. And in listening to the responses of both you and Mr. Shaw to questions asked by my colleagues, I have a series of questions that I was going to ask, but obviously I am not going to get answers to them, so I am not going to ask them. What I would like to have for the committee record, hopefully within 1 week if we can, is something from Mr. Shaw as I understand it he is the one who did the calculation on this as to how exactly he got to the 50 cents and how we are where we are. In all your testimony, you went around Robin's barn but you never got into the barn. We want to know how you came up to the 50 cents and see if we can follow it.

I could ask a series of questions here, but I just don't think it has been developed. I would like to have it for the record. I assume Mr. Shaw is the one who has the responsibility for it in your shop. If he can provide it or you can provide it, I would appreciate it.

Mr. GOLDBERG. Congressman, are you talking about the 50-cent reduction in support?

Mr. COELHO. Yes, the 50-cent reduction. How you came up with your figures.

Mr. GOLDBERG. You mean why we made that decision?

Mr. COELHO. How you came up with—most of us up here feel that you went beyond 50 cents.

Mr. GOLDBERG. Oh, Congressman.

Mr. COELHO. As a matter of fact, I will announce something in 1 minute that will tell you how serious we think it is, but we do feel you went beyond 50 cents and we want to see the data that shows us how you came up with your figures.

Mr. GOLDBERG. Congressman, we have published the data on how we arrived at those calculations.

Mr. COELHO. OK. Everything that we have seen tells us that you have gone over the 50 cents, and if you don't have something other than what we have seen, then you don't need to comply with my request.

Mr. GOLDBERG. We will be glad to comply with your request, Congressman, but we have not gone over the 50 cents.

[The information follows:]

The following table shows the total calculation used to implement the April 1 changes.

It shows value of butter and Nonfat Dry Milk dropping from $13.82 to $13.32 and the values of cheese and whey from $13.97 to $13.47—in each case a drop of 50 cents.

CALCULATION OF CCC PURCHASE PRICES FOR DAIRY PRODUCTS WITH SUPPORT AT $12.60 AND $12.10 PER CWT.

Item	Effective December 1, 1983-March 31, 1985	Effective April 1, 1985
Support price for manufacturing milk, $/cwt. at 3.67% milkfat	12.60	12.10
Support price for manufacturing milk, $/cwt. at 3.5% milkfat	12.31	11.81
Average milkfat test, percent	3.67	3.67
Butterfat differential	17.2 1/	17.2 2/
Yields per 100 pounds of milk at average test (pounds)		
Butter	4.48	4.48
Nonfat Dry Milk	8.13	8.13
Cheese	10.1	10.1
Butter-Nonfat Dry Milk Calculation		
Return to butter-powder plants, $/cwt.	12.60	12.10
CCC manufacturing allowance for converting 100 pounds of whole milk into butter and NDM, $/cwt.	1.22	1.22
Value of butter and NDM (U.S. average) made from 100 pounds of milk, $/cwt.	13.82	13.32
Calculation December 1, 1983		
NONFAT DRY MILK PURCHASE PRICE, $/lb.	.91	
Value of NDM per 100 pounds of milk, $/cwt. 3/	7.40	
Value of Butter (residual):		
Dollars per 100 pounds of milk	6.42	
Dollars per 100 pound at Chicago (calculated) 4/	1.4330	
BUTTER PURCHASE PRICE at New York, $/lb.	1.4625	
BUTTER PURCHASE PRICE, at Chicago, $/lb. 5/	1.4325	
Calculation April 1, 1985		
BUTTER PURCHASE PRICE, $/lb. 6/		1.4325
Value of butter per 100 pounds of milk, $/cwt.		6.42
Value of nonfat dry milk (residual):		
Dollars per 100 pounds of milk		6.90
Dollars per pound (calculated) 7/		.8487
NONFAT DRY MILK PURCHASE PRICE (rounded), $/lb.		.8475
Cheese Price Calculation		
Return to cheese	12.60	12.10
CCC manufacturing allowance for converting 100 pounds of whole milk into cheese and whey, $/cwt.	1.37	1.37
Value of cheese and whey/per 100 pounds of milk, $/cwt.	13.97	13.47
Value of whey:		
.25 pounds of fat, $ 8/	.36	.36
Other solids, $	.00 9/	.10 10/
Total, $	.36	.46
Value of cheese:		
Dollars per 100 pounds of milk	13.61	13.01
Dollars per pound (calculated) 11/	1.3475	1.2881
CHEESE PURCHASE PRICE (rounded), $/lb.	1.3475	1.2875

1/ Butter purchase price at Chicago times 0.12.
2/ Butter purchase price times 0.12
3/ NDM price per pound times 8.13.
4/ Value of butter per 100 pounds of milk divided by 4.48.
5/ Price at Chicago is based on estimate of freight rate effective October 1, 1983, but limited to the maximum 3¢ reduction from the New York price.
6/ Single nationwide butter purchase price. (Maintained Chicago butter purchase price and allocated entire decrease in support price to nonfat dry milk.)
7/ Value of nonfat dry milk per 100 pounds of milk divided by 8.13.
8/ Butter purchase price at Chicago times 0.25.
9/ Estimated that 70 percent of whole milk cheese whey solids other than fat is processed at 0¢ net return.
10/ Estimated that 70 percent of whole milk cheese whey solids other than fat (5.5 pounds per cwt. of whole milk) is processed at a 2.5¢ per pound net return (15.0¢ dried whey average price minus 12.5¢ processing costs):
[.70 (5.5 x 2.5) = .70 (13.75)= 9.625 = 10¢/cwt. (rounded)]
11/ Value of cheese per 100 pounds of milk divided by 10.1.

ASCS-DAD:4-3-85:0202D

Mr. Coelho. We will find out for sure on that.

Mr. Lewis, do you have any questions before we go on?

Mr. Lewis. Not at this time, thank you.

Mr. Coelho. I would like to announce that Mr. Jeffords and I will be asking for an investigation by the General Accounting Office and they will report back to this subcommittee whether you have exceeded your authority under the law so that this subcommittee can act accordingly. We feel it is critical to the future of dairy policy, particularly as we face the possibility of another price cut on July 1. Congress must ensure that the intent of the law is complied with and that each of these price cuts is not in excess of what Congress has authorized; 50 cents is what we authorized and only 50 cents.

We will be also requesting the same of the inspector general.

[The letters follow:]

TONY COELHO, CALIFORNIA,
CHAIRMAN

HAROLD L. VOLKMER, MISSOURI
JAMES R. OLIN, VIRGINIA
TIMOTHY J. PENNY, MINNESOTA
CHARLES ROSE, NORTH CAROLINA
CHARLES W. STENHOLM, TEXAS
TOM DASCHLE, SOUTH DAKOTA
ED JONES, TENNESSEE
BERKLEY BEDELL, IOWA
GLENN ENGLISH, OKLAHOMA

E (KIKA) DE LA GARZA, TEXAS,
EX OFFICIO MEMBER

KIM SCHNOOR
STAFF DIRECTOR

U.S. House of Representatives
Committee on Agriculture
Subcommittee on Livestock, Dairy, and Poultry
Room 1301, Longworth House Office Building
Washington, DC 20515

JAMES M. JEFFORDS, VERMO
RANKING MINORITY MEM

LARRY J. HOPKINS, KENTUCK
ARLAN STANGELAND, MINNE
STEVE GUNDERSON, WISCON
TOM LEWIS, FLORIDA
ROBERT F. (BOB) SMITH, ORE

EDWARD R. MADIGAN, ILLINO
EX OFFICIO MEMBER

*STEPHEN R. KERR
MINORITY CONSULTANT

May 21, 1985

Honorable John V. Graziano
Inspector General
U.S. Department of Agriculture
Washington, D. C. 20250

Dear Mr. Graziano:

On behalf of the Subcommittee on Livestock, Dairy, and Poultry of the House Agriculture Committee, we request that you evaluate the United States Department of Agriculture's implementation of the April 1 price cut in the national support price for milk.

The Secretary of Agriculture was authorized to reduce the price support by 50¢ on April 1, 1985, pursuant to the Dairy and Tobacco Stabilization Act of 1983. Based on the research of our staff and the testimony which was heard at a hearing today from various people in the dairy industry, we have reason to believe that the Secretary may have exceeded this authority and implemented a price cut in excess of 50¢.

Accordingly, we request that you investigate this matter and report your findings to us by June 15, 1985. We are facing the possibility of another price cut on July 1, 1985, and it is essential that we determine if the Secretary has exceeded his authority prior to that time.

We greatly appreciate your cooperation in this matter.

Sincerely,

James M. Jeffords
JAMES R. JEFFORDS
Ranking Minority Member

Tony Coelho
TONY COELHO
Chairman

TONY COELHO, CALIFORNIA,
CHAIRMAN

HAROLD L. VOLKMER, MISSOURI
JAMES R. OLIN, VIRGINIA
TIMOTHY J. PENNY, MINNESOTA
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ROBERT F. (BOB) SMITH, OREGON

EDWARD R. MADIGAN, ILLINOIS
EX OFFICIO MEMBER

*STEPHEN R. KERR
MINORITY CONSULTANT

May 21, 1985

Honorable Charles A. Bowsher
Comptroller General of the
United States
General Accounting Office Building
441 G Street
Washington, D. C. 20548

Dear Mr. Bowsher:

On behalf of the Subcommittee on Livestock, Dairy, and Poultry of the House Agriculture Committee and pursuant to Title 31, §717 of the United States Code, we request that you evaluate the United States Department of Agriculture's implementation of the April 1 price cut in the national support price for milk.

The Secretary of Agriculture was authorized to reduce the price support by 50¢ on April 1, 1985, pursuant to the Dairy and Tobacco Stabilization Act of 1983. Based on the research of our staff and the testimony which was heard at a hearing today from various people in the dairy industry, we have reason to believe that the Secretary may have exceeded this authority and implemented a price cut in excess of 50¢.

Accordingly, we request that you investigate this matter and report your findings to us by June 15, 1985. We are facing the possibility of another price cut on July 1, 1985, and it is essential that we determine if the Secretary has exceeded his authority prior to that time.

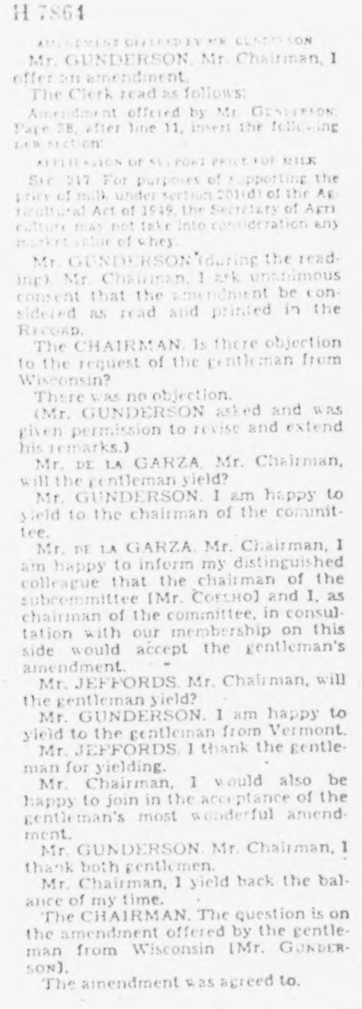
We greatly appreciate your cooperation in this matter.

Sincerely,

James M. Jeffords
JAMES R. JEFFORDS
Ranking Minority Member

Tony Coelho
TONY COELHO
Chairman

It should be noted that an amendment was included in H.R. 2100, the Food Security Act, which responded to the findings of the Office of Inspector General and Government Accounting Office investigations. This amendment was adopted on September 26, 1985 and H.R. 2100 passed the House of Representatives on October 8, 1985. The amendment and floor discussion is as follows from the Congressional Record, September 26, 1985:



H 7864

AMENDMENT OFFERED BY MR. GUNDERSON

Mr. GUNDERSON. Mr. Chairman, I offer an amendment.

The Clerk read as follows:

Amendment offered by Mr. GUNDERSON: Page 78, after line 11, insert the following new section:

APPLICATION OF SUPPORT PRICE FOR MILK

SEC. 217. For purposes of supporting the price of milk under section 201(d) of the Agricultural Act of 1949, the Secretary of Agriculture may not take into consideration any market value of whey.

Mr. GUNDERSON (during the reading). Mr. Chairman, I ask unanimous consent that the amendment be considered as read and printed in the RECORD.

The CHAIRMAN. Is there objection to the request of the gentleman from Wisconsin?

There was no objection.

(Mr. GUNDERSON asked and was given permission to revise and extend his remarks.)

Mr. DE LA GARZA. Mr. Chairman, will the gentleman yield?

Mr. GUNDERSON. I am happy to yield to the chairman of the committee.

Mr. DE LA GARZA. Mr. Chairman, I am happy to inform my distinguished colleague that the chairman of the subcommittee [Mr. COELHO] and I, as chairman of the committee, in consultation with our membership on this side would accept the gentleman's amendment.

Mr. JEFFORDS. Mr. Chairman, will the gentleman yield?

Mr. GUNDERSON. I am happy to yield to the gentleman from Vermont.

Mr. JEFFORDS. I thank the gentleman for yielding.

Mr. Chairman, I would also be happy to join in the acceptance of the gentleman's most wonderful amendment.

Mr. GUNDERSON. Mr. Chairman, I thank both gentlemen.

Mr. Chairman, I yield back the balance of my time.

The CHAIRMAN. The question is on the amendment offered by the gentleman from Wisconsin [Mr. GUNDERSON].

The amendment was agreed to.

Mr. Coelho. Mr. Goldberg, we are serious about that. This is why we have requested the hearing. The data that we have come up with with our staff and our staff has dealt with the people in the Department, the information that I have seen, I think that you have gone over it and substantially over it, not just a cent or two over the 50 cents.

Now, you can leave out the transportation or you can leave out something else and make your justification, but whatever it is, we feel you have gone over it. If you have, you are going to hear a lot from us, and we will question you further on it. I think it is important that this matter be resolved quickly before July 1 so we know how you did it and what the impact has been. If it has been 50 cents or under, we will say so and you won't hear any critical things from us, at least on reaching that amount. But if you have gone over it, which we suspect you have, you are going to hear a lot from us.

Mr. Volkmer.

Mr. Volkmer. Mr. Goldberg, CCC butter purchases exceed nonfat dry milk, do they not, as far as cost?

Mr. Goldberg. Do butter purchases exceed it in terms of cost?

Mr. Volkmer. Yes. Haven't they gone up since April 1 in proportion to NDM?

Mr. Goldberg. Yes, Congressman. The answer to your question is yes, and the reason is because we lowered the support on nonfat dry milk and did not on the butter portion.

Mr. Volkmer. Doesn't it cost the CCC more now to buy up all this——

Mr. Goldberg. No. On the contrary, we should be having some cost savings. That was the purpose, because we were buying far more, relatively, more nonfat dry milk than we were butter. I have forgotten the percentage.

Mr. Volkmer. I have to wait and see the calculation, because we don't have the dollar amounts in here, and I would like to see the dollar amounts.

Mr. Goldberg. We have, I think, percentage/proportion amounts in the testimony, Congressman.

Mr. Volkmer. All I have is the total amounts purchased in 2-week time periods, April 1 to 15, 16 to 30, and May 1 to 15. Those are in pounds but not in dollars.

Mr. Goldberg. Last year, Congressman, we were buying, according to our numbers here, 3½ times more powder than butter, and now we are down to 1.9 to 1 in the first 15 days of May.

Mr. Volkmer. Well, what is the price differential to CCC?

Mr. Goldberg. I don't have that, Congressman.

Mr. Volkmer. I mean, is it cheaper to buy butter than nonfat dry milk?

Mr. Goldberg. If you are talking about on a per pound basis, butter is more expensive, but you are not really comparing apples with apples.

Mr. Volkmer. Well, if I increase butter purchases by, say, 11,000 pounds and only decrease nonfat dry milk by 2,000 or 3,000 pounds, it appears to me that I have increased cost and not decreased cost. I would appreciate it if you could furnish us with the total costs of the program, what it is now costing us as against 1984 on those same products.

Mr. GOLDBERG. I can give you, Congressman, some calculated cumulative weekly costs for the two items. I would be glad to do that.

Mr. VOLKMER. I would appreciate that.

Thank you, Mr. Chairman.

Mr. COELHO. Thank you, Mr. Volkmer.

Are there any other questions?

[No response.]

Mr. COELHO. Thank you. We appreciate your testimony, and you will be hearing more from us.

We would like to have the first panel come up: Dr. Cropp, Mr. Anderson, Neal Bjornson, and James Tillison. Dr. Cropp, you may start.

STATEMENT OF ROBERT A. CROPP, PROFESSOR AND AGRICULTURAL MARKETING SPECIALIST, EXTENSION, UNIVERSITY OF WISCONSIN-PLATTEVILLE

Mr. CROPP. Thank you. My name is Robert Cropp. I am with the University of Wisconsin Extension, University of Wisconsin-Platteville.

I thank you for inviting me to testify at this important hearing today. I have a copy of my remarks that I would like to have for the record, and I will highlight them.

Mr. COELHO. Without objection, so ordered.

Mr. CROPP. As has been indicated already, it has been charged that the new CCC purchase prices will actually result in more than a 50 cent reduction in farm milk prices. Some charge that farm milk prices will fall more than 70 cents per hundredweight; that is, more than 20 cents below the $12.10 April 1 support price.

The more than 70 cents per hundredweight may be too strong. However, I think a reduction somewhere between that 50 to 70 cents per hundredweight appears to be valid. I will explain the basis for my conclusion, but first I would like to just quickly review the intent of the dairy price support program as authorized by the Agricultural Act of 1949.

The Ag Act of 1949 and amendments to that act specified three major guidelines for the operation of the price support program. The first two are not at issue today, so I will just briefly mention them. The first one is to provide for minimum and maximum levels at which farm milk prices were to be supported. The second one is that the program authorized the Secretary of Agriculture to determine the specific price within these minimum and maximum prices specified in the legislation with the objective to ensure an adequate supply of milk.

The third guideline is the one we are really dealing with today.

Mr. COELHO. Mr. Cropp.

Mr. CROPP. Yes.

Mr. COELHO. Excuse me a minute, but is Mr. Shaw or Mr. Goldberg in the room? Neither one of them stayed? Will staff encourage them to stay? Maybe we can find out what is really going on here if they have the decency to stay.

Go ahead, Dr. Cropp.

Mr. Cropp. The third guideline is the one that we are dealing with today which says that the specified price would be supported through purchases of milk and milk products. Since milk is a bulky and perishable product, the Government cannot buy raw milk. Therefore, it purchases butter, nonfat dry milk, and cheese offered by processors at announced prices.

The issue here is that these purchase prices are set at levels designed to enable manufacturers of these dairy products to pay farmers the announced support price for milk in surplus production periods. As announced April 1, the CCC purchase prices fail to meet this guideline for the following reasons.

The first one is the manufacturing or make allowance on margins to cover the costs of processing milk into butter-powder and cheese is used to calculate the CCC purchase prices. The make allowances have not been increased since 1979. With increases in plant operating costs since then, energy, labor, packaging, et cetera, it may be difficult for some plants to pay the April 1, 1985, support price of $12.10.

The second reason is that the CCC purchase prices before and after April 1, 1985, as shown in the table and we all know what they are—on the right-hand column I express it in terms of milk equivalents.

The new purchase prices for butter and nonfat dry milk appear to be in line with a 50 cent reduction in the support price. Nevertheless, there still is a concern with the butter-powder. All the 50-cent cut for butter-powder was placed on nonfat dry milk. This does not help butter's competition with oleomargarine. In addition, previously, a CCC purchase price was determined for both Chicago and New York. The Chicago butter price was 3 cents per pound less than New York. The purchase price reflects some difference in freight costs from Chicago.

As of April 1, the New York price was lowered 3 cents and there was no change in the Chicago price. We have now one national CCC purchase price of $1.4325 per pound. This may put Chicago butter at some competitive disadvantage to New York butter and could in fact impact on farm milk prices in Minnesota and Wisconsin, major butter producing areas.

The third concern is really the one I think of major issue today. That is the concern over the April 1, CCC purchase price with cheese. With a yield of 10.1 pounds of cheese per 100 pounds of milk used in CCC calculations, one would expect a 50 cent drop in the support price would reduce the CCC purchase prices about 4.9 cents per pound. However, the decrease was 7.25 cents for barrel and 6 cents for blocks.

The justification for this drop in cheese purchase prices was based upon an assumed net return or profit in whey solids-not-fat. A value for the fat in whey has been used in calculating CCC purchase prices for cheese, but never before was a net value assumed on the solids-not-fat in whey. I think this is the key issue in today's hearing.

A value of about 36 cents per hundredweight of milk used for cheese attributed to the fat in whey appears valid. Fat in whey of about 0.25 pound per 100 pounds of milk may readily be removed and used to make whey cream butter. Thus, a quarter of a pound of fat times the current butter price would yield around 36 cents per hundredweight. Thus, with a net return of that amount on fat in whey of 36 cents per hundredweight, the CCC purchase price of cheese may be lowered accordingly and still enable the cheese plants selling to the CCC to pay farmers the support price.

However, an assumed value of 10 cents per hundredweight of milk for whey solids-not-fat is questionable for the following reasons. There are, for example, around 287 cheese plants in the State of Wisconsin but only 31 dry whey plants. Only half of these are capable of making the dry whey for human use which commands a price of about 15 cents per pound. In addition, the majority of the whey drying plants are owned and operated by barrel cheese plants that are capable of selling to the Government.

Based on some of my looking into this here, even these operators indicate that assumed net return of 2.5 cents per pound for dry whey may be high. Thus, the majority of the cheese plants, especially the smaller plants, are not receiving a net return or profit from their whey, but they actually have a net cost of disposing of the whey. Thus, the assumed value of 10 cents per hundredweight of milk attributed to whey solids-not-fat in calculating the April 1, 1985, purchase price for cheese appears too high.

Another concern is the spread of 4.25 cents per pound between barrel and block cheese. In the past, this spread has been 3 cents per pound, as has been indicated. The spread of 4.25 cents per pound may be too large and places barrel cheese plants at a disadvantage to blocks.

Although the spread between barrels and blocks has averaged 4.26 cents per pound on the National Cheese Exchange at Green Bay, WI, as indicated by USDA, this is not justification for the 4.25 cent spread.

The cheese industry uses reusable steel barrels for cheese not sold to CCC. The CCC, however, only purchases cheese in nonreusable fiber barrels. This adds to the cost of barrel cheese of about $5 per barrel or 1 cent per pound of cheese. Therefore, the spread between barrels and blocks appears to still be 3 cents per pound and not the 4.25 cents. As a result, barrel cheese appears to be at a price disadvantage to block cheese.

A fifth concern is that starting on April 1, CCC will no longer pay a premium for barrel cheese below 34 percent moisture. A typical cheese plant turns out barrel cheese between 32 and 32.5 percent moisture. Higher moisture cheese will age faster and break down faster. In addition, higher moisture cheese is likely to contain more free whey which is not desired by the CCC. Thus, the 34 percent moisture level is not as attractive or creates some problem for barrel cheese producers.

The sixth concern is that with barrels then at a disadvantage to blocks, barrel prices will be depressed and this will eventually lower block prices as plants either sell more barrels on the commercial market rather than to the CCC or shift from barrel to block production. Thus, all cheese prices may drift lower, and so will the price per 100 pounds of milk utilized for cheese.

Lastly, the claim that April 1, CCC purchase prices will result in more than a 50-cent-per-hundredweight drop in farm milk prices may be substantiated by what has actually happened to product prices in recent weeks. On page 5, I summarize the current wholesale prices for butter and cheese, and you can see they are well below 20 cents per hundredweight.

In summary, if you look at what has happened in the April Minnesota-Wisconsin price series for 3.5 percent test milk, it was $11.62 per hundredweight which is 33 cents for March and 78 cents down from January and is 20 cents below the current support price of $11.82 for 3.5 test.

[The prepared statement of Mr. Cropp appears at the conclusion of the hearing.]

Mr. COELHO. Thank you. That is very interesting testimony, particularly when you compare it to what the Department just said.

Mr. Anderson.

STATEMENT OF ROBERT F. ANDERSON, EXECUTIVE DIRECTOR, NATIONAL CHEESE INSTITUTE AND AMERICAN BUTTER INSTITUTE

Mr. ANDERSON. Thank you, Mr. Chairman.

Mr. COELHO. Mr. Anderson, excuse me for a moment. Mr. Volkmer just told me that he had not announced that the testimony is limited to 5 minutes, so we would appreciate your limiting your testimony to 5 minutes and summarize your statement. Whatever statement you have will be made a part of the record. We want to get everybody in, and we want to adjourn at a decent hour.

Mr. ANDERSON. Yes, sir, I would appreciate it, however, if I could speak for both the butter industry and the cheese industry which will take 10 minutes possibly. I realize I am one person, but I do speak for two very important industries that have a very important stake in this particular hearing. I will try very much to limit it.

Mr. COELHO. We will limit you to 5 minutes, and you will find that we are going to pursue this case, so don't oversell when you have somebody going your way.

Mr. ANDERSON. I hope not, sir. Thank you.

I am Robert F. Anderson, executive director of the National Cheese Institute and the American Butter Institute. ABI and NCI members represent over 80 percent of the butter and cheese marketed in the United States and, most important, they represent two of the three products which are the subject of today's hearing, the impact of the April 1 dairy support announcement on the nonfat dry milk, butter, and cheese industries.

First of all, I have prepared two charts for you to review. An analysis of these charts shows that the sales of butter and cheese to CCC in April reversed the 1985 trend which had been one of reduced sales relative to 1984. For example, table 1 shows that butter sales to CCC in April compared to April 1984 increased from 20 million to 30 million pounds.

Cheese in 40-pound blocks and 500-pound barrels jumped from 49 million pounds in 1984 to 63 million pounds in 1985. Two-thirds of the increase was in the more expensive 40-pound block styles, reflecting the Government's action taken April 1 to discourage the sales of the less expensive bulk barrel cheese.

Interestingly, there was very little year to year change in CCC purchases of nonfat dry milk which increased from 71 to 72 million pounds.

These facts indicate that the Government action on April 1 have seriously disrupted the butter and cheese markets. Of greater concern, in doing so, the cost of the program to the Government has escalated up instead of staying on the downward path established earlier in the year.

In April, alone, the Government spent $14 million more to support butter than a year earlier. Compare this to the $1.5 million increase in NDM purchases from April 1984 to April 1985. It is difficult for me to understand how the Department of Agriculture can say that this $13 million increase is going to eventually have a reduction in cost of $37.5 million. I think that answers one of your questions, sir. This cost reduction in NDM purchases was given in the USDA position paper which purports to justify refusing to allocate a proportionate share of the support price decrease to butter.

Compare the events of April to January. In January 1985, under the former pricing structures, CCC purchased 11 million pounds less butter than in January 1984, a savings to the Government of approximately $16 million. Sales of NDM were also down and the Government saved $15 million over January 1984.

It would seem a review of the facts and events to date would indicate the USDA made a serious error in judgment by allocating an entire reduction to NDM and none to butter.

The purpose of the dairy support program is to provide an adequate supply of whole milk. To carry out this program, the Government purchases certain dairy products if and when they become surplus by assigning to butter, NDM, and cheddar cheese fair and equitable prices. The Government should not attempt to manipulate the market to its own purposes and ignore the commercial market, and if it does so, it does so at its own peril.

The April 1 actions regarding cheese are a classic example of Government blundering into a market situation without taking into account the mechanics of the market.

Bulk cheese from the manufacturer is made and packaged so it can be stored for future processing in an efficient and economical manner. One of the factors that ensures this condition is a reasonably low moisture, the lower the better. The moisture content is self-controlling, because if the cheese does not have sufficient moisture, it will not meet the desired top U.S. grade standards for flavor, body, and texture.

Cheese evolved over the centuries as a practical way of storing milk solids for future use. It should be understood that the pounds of cheese obtained from 100 pounds of milk decreases as the amount of moisture decreases. Further, the amount of solids in the cheese are the valuable constituents and industry charts have been developed to prove it. We have determined the value of a pound of cheese at various moisture levels.

Taking the April 1 barrel cheese support price of $1.2450, the calculations are as follows. You get about 10.1 pounds of cheese at 39 percent moisture. At $1.2450, that equals $12.57 per 100 pounds of milk.

9.4785 pounds of cheese at 35 percent moisture at $1.3266 per pound equals $12.57.

9.1955 pounds of cheese at 33 percent moisture at $1.3765 per pound equals $12.57 per 100 pounds of milk.

So, you see there is no premium in there. They are paying the same amount for 100 pounds of milk regardless, and the price paid for this milk is the same. That is no premium payment.

However, the April 1 limitation of 34 percent on moisture adjustment is $1.3470. The value per 100 pounds of milk for 33 percent moisture cheese is now only $12.38. This is the same as a 19 cent per hundred reduction in the support price of milk, clearly not the intent of the law. The Government should pay for what it gets, no more and no less.

Even so, the handling costs to the Government are increased as the moisture content of the cheese is increased. For example, if the moisture is increased just 2 percent, say from 33 to 35 percent, there will be an additional 11 pounds of water in each barrel. In a 112,000 pound carlot, which is normal, there will be four extra barrels to be packaged, handled, shipped, stored, and finally processed.

This extra moisture limits the length of time the cheese may be stored. Recall, the lower the moisture, the longer the cheese will maintain its quality.

Finally, when that carlot of 33 percent and carlot of 35 percent cheese are processed, the pounds of processed cheese resulting from either lot will be the same because the pounds of solids are the same. So, there is no rational basis for the Government's action in this particular instance. They should eliminate the lower level.

The April 1 announcement, in a separate action, increased the price spread between barrel and block cheese from 3 to 4.25 cents. Table 2 shows that for the same ratio of barrel to block cheese sales to CCC has been about 3 or 4 to 1. In April, it dropped to roughly 2 to 1. The USDA signals were clearly heard. Now, the Government has more tonnage of expensive block cheese that may not store as well as barrel cheese and is more expensive to eventually process.

The most unfortunate aspect of this situation is that the National Cheese Exchange rules outlined this problem long before, and the USDA should have known about it.

Whey is the liquid portion of milk remaining after the cheese is made. I want to be sure to get this in if that light goes out. You have to remember that the more acid the whey is, the less valuable it is. Swiss cheese whey and mozzarella whey are very valuable. The figures that the USDA were quoting were based upon Swiss cheese whey and mozzarella whey. Cheddar whey is an acid whey, and it has minimum if any commercial utilization and value. The USDA, however, lumped the whey from all cheese into one calculation and assumed a value that is not representative of cheddar cheese, the product for which the support program is settled, and they assigned that value to it.

We have surveyed our members and find that the average value of cheddar whey over processing costs is not more than 1 cent per pound. The adjustment for cheddar whey should therefore be between 0 to not more than .03, not 10 cents.

I guess my next point is that what we really need here is more teamwork between the U.S. Department of Agriculture and the industry. Bless their hearts, they are trying to do the job alone. We are here to help them. They are going 1 on 1 when they need teamwork.

The red light is on. I have a lot more to say. I hope you will get a chance to read it.

[The prepared statement of Mr. Anderson appears at the conclusion of the hearing.]

Mr. COELHO. We are going to have some questions for you, and you will have a chance to say it then.

Neal.

STATEMENT OF NEAL R. BJORNSON, ASSISTANT TO THE GENERAL MANAGER, ASSOCIATED MILK PRODUCERS, INC.

Mr. BJORNSON. Thank you, Mr. Chairman.

I am Neal Bjornson, assistant to the general manager of Associate Milk Producers, Inc. We appreciate the committee's concern over the impact of the April 1, dairy price support adjustment and this opportunity to comment on its effect. I particularly want to thank you, Mr. Chairman, for the action you and Congressman Jeffords have announced this afternoon in furthering this effort.

At the outset, I should state that prior to April 1, AMPI submitted a series of comments to Secretary Block recommending several actions with respect to the dairy price support program. Foremost among these was a recommendation that the price support reduction authorized for April 1 not be made.

USDA's recent studies of the financial conditions of farmers in general, and dairy farmers in particular, make clear a pattern of steadily deteriorating financial capacity. In 1984, over one-fourth of all dairy farmers had debt to asset ratios in excess of 40 percent. Discussions with farm lenders and dairy farmers themselves indicate that this pattern has not been reversed and that departures from dairying in many areas have accelerated.

Based on this, it was recommended that no reduction in the price support level be made April 1. In the interest of maintaining needed supplies of milk and dairy farm family operations, we make a similar recommendation with respect to the reduction authorized July 1.

Notwithstanding our recommendation, Secretary Block did announce a 50 cent price support reduction effective April 1. In the process of establishing the product purchase prices on which that decision was to be implemented, a number of actions were taken which effectively increased the reduction.

The dairy price support program is implemented through Commodity Credit Corporation purchases of specific dairy products at announced prices. The adequacy of those prices determine the ability of processors to meet their costs and return the announced price support level to the farmer in payment for milk. The effective reduction in price support level can be measured by the reduced ability of product manufacturers to pay farmers for milk.

Tables 1 and 2 attached to my submitted statement demonstrate the effect of the April 1 action. The bottom line in this case is that the processors' ability to pay farmers for milk was reduced anywhere from 51 to 74 cents per hundredweight, depending on the products produced from the milk, the area of the country, or the strength of certain by-product markets. This analysis is based on USDA's yields and the prices for products that were in effect under the price support program before April 1 and after April 1.

This reduction, the 50 cent reduction, or supposed 50 cent reduction, in the price support level, was accompanied by a continuation of a policy that has prevented achievement of the announced price support level over most of the past 4 years. The processing margins used in determining product purchase prices are $1.22 per hundredweight for milk going into butter-nonfat dry milk production and $1.37 for cheese. These processing margins were established in October 1979.

A plant survey by the National Milk Producers Federation earlier this year determined the costs in butter-nonfat dry milk plants have risen 45 percent since 1979. In cheese plants, the average increase runs 30 percent. Based on these findings, AMPI has recommended that the Secretary increase the processing margin for milk made into butter-nonfat dry milk by 40 cents per hundredweight and for cheese milk by 30 cents.

Mr. Chairman, at this time, we would make several specific recommendations. First, an early announcement should be made by the Secretary of Agriculture indicating that the authorized July 1 price support reduction will not be made. We are viewing at the present time demoralized product markets and can expect to continue until after July 1 because of the anticipated price support reduction.

Second, immediate action should be taken to correct the inequities created which resulted in the value of the April 1 action exceeding 50 cents.

Third, an immediate increase should be announced in the processing margins used in determining CCC product purchase prices.

Fourth, other administrative actions with respect to the dairy price support program which would have the effect of reducing farm income should be avoided. In this respect, I would call particular attention to the possibility of reduced CCC sell-back levels in connection with any July 1 price support action. Thank you.

[The prepared statement of Mr. Bjornson appears at the conclusion of the hearing.]

Mr. COELHO. Thank you, Neal. I appreciate your staying within the allotted time.

Mr. Tillison.

STATEMENT OF JAMES E. TILLISON, EXECUTIVE DIRECTOR, WISCONSIN CHEESE MAKERS ASSOCIATION

Mr. TILLISON. Thank you, Mr. Chairman.

My name is Jim Tillison. I am the executive director of the Wisconsin Cheese Makers Association. The association represents 175 manufacturers and wholesalers of cheese and butter in 12 States. Of those 175 members, 150 operate cheese factories.

The WCMA believes that the USDA formulation of the April 1 CCC purchase price for cheddar cheese and the adjustment made to the cheddar block-barrel differential have essentially lowered cheese prices to the point where the net effect on producers' pay prices will be more than the 50 cent reduction Congress intended.

Let's look at the whey credit first. The key question here is, do cheese plants actually get a net margin, that is, selling price less costs, for their whey of 10 cents per hundredweight of milk that they can return to the dairymen? A member survey by the WCMA clearly indicates the answer is no. We sent out a questionnaire to our members and we asked them a very simple question: Do you get no return for your whey, 1 to 5 cent net return for your whey, 6 to 9 cents net return for your whey, or a 10 cent or more return for your whey?

Of the 52 percent of our members that responded, only 10.3 percent said they got 10 cents. 88.5 percent said they got 5 cents or less. As a matter of fact, 70.5 percent stated they got nothing in return for their whey. In fact, a couple of questionnaires had a little comment in them which said, it costs me 15 cents to dispose of the stuff.

The USDA, in their actions, did not just impact the people who sell cheese to the Government. There is a very simple reason for that. The cheese industry looks to a commodity market that is called the National Cheese Exchange for its pricing. The entire industry uses this market as a basis for selling and buying product. Cheeses other than cheddar are priced at so many cents over or so many cents under the market's block price.

The National Cheese Exchange reacts to what the Government does with its purchase prices. Therefore, when the Government purchase price moved down 6 cents, the National Cheese Exchange responds to that, and it moves down 6 cents.

As I said before, cheese plants are not getting a return for their whey. The vast majority of cheese plants are getting nothing; 90 percent are getting less than 10 cents. In fact, as I said, 88.5 percent are getting 5 cents or less for their whey.

The other thing to consider is that when you look at the cheese formula and when you look at the butter-powder formula, whey is the only product that is not supported by Government purchase. That means that it is subject to the volatility of the marketplace, and you can ask anyone who has been in the whey business whether it is a volatile market or not. It is. In addition to that, it is directly impacted by milk protein imports. So, we feel that for these reasons, the WCMA urges the Congress to work for the immediate removal of this factor from the cheddar cheese support price calculation.

Now, let's look at the barrel-block price spread. The USDA said that they observed an average of 4 to 4.5 cents in the marketplace on the difference between block and barrel cheese. They came up with a figure of 4.25 cents. If you look at industry publications, for example, Wisconsin report prices, they will have a notation that says barrels returned. That means that steel barrels are being traded.

The National Cheese Exchange price carries no such notation, but if one is aware of the rules of the Exchange, or if they would just call the Exchange's president, they would learn that the seller has the option of filling the sale with either steel barrels which are returnable or fiber barrels. If they sell fiber barrels, they essentially bill the buyer 1 cent per pound more.

Now, I averaged the 52 weeks in the National Cheese Exchange price and came up with an average spread of 4.34 cents. This is in 1984. If you take out the 2 weeks where the spread was below 5 cents and the 9 weeks where the spread was above 5 cents, the Cheese Exchange price differential was 3.97 cents. Subtract the 1 cent for the fiber barrel cost, and you have a 3 cent spread in the commercial marketplace.

I believe that the USDA was not aware of this situation and, therefore, made an incorrect evaluation of the industry when they did this spread.

Finally, I can only reiterate what Mr. Anderson says about the moisture premium. You can't dispute the fact that if you don't pay for less than 34 percent moisture, you are going to save money. However, the industry will then shoot for 34 percent moisture as the minimum level. When you increase moisture, you increase yield. When you increase yield, you increase the amount of cheese and volume that the Government buys.

For example, in 1984, the Government would have bought, if you increased the moisture premium 1 cent, the Government would have bought 5,000 more barrels of cheese which, essentially, would have all been water.

Thank you very much.

[The prepared statement of Mr. Tillison appears at the conclusion of the hearing.]

Mr. COELHO. Coming from an area of California where water is so precious and where we pay a lot for it, it is kind of interesting that the Government is buying it now. Maybe we ought to have a program of recycling it back out to water deficient areas.

I think what we should do, if the members agree, is to go vote. If the panel will be patient, we will quickly vote and we will come right back and proceed with the questioning.

[Recess taken.]

Mr. COELHO. Between the figures that you come up with and those that the USDA has come up with, it doesn't seem to make much sense. Somebody is not talking to somebody. Have you talked to them? What do they say to you? How can you be so far apart?

Mr. TILLISON. One of the things that we found interesting was, for example, we talked to the president of the National Cheese Exchange. Did the USDA contact them? No. We talked to the executive director of the Whey Products Institute. Have there been any lengthy discussions with them? No. They didn't call me, and I don't think they called anybody on this panel.

Mr. COELHO. Did they call anybody on the panel?

Mr. ANDERSON. Mr. Chairman, they didn't call. I did sit down with them, and we did talk to them about many of these things beforehand and objected to them, in particular, the whey situation. I pointed out to them at that time and we did give them some figures that the value of cheddar whey is less than some of these others. They went ahead and did it on their own.

We have talked to them, yes. I think we should not assume that they don't—or that I am not trying to find out what they are trying to come up with, what actions they are trying to take. So, we do talk to them. The problem is that they don't listen.

Mr. BJORNSON. Mr. Chairman, we do, of course, talk to people in the Department, both at the policy level and the staff level routinely. I think it is interesting in this particular instance. In the past, prior to a price support announcement, there has been normally an invitation published for comment listing points that are under consideration and asking for recommendations on specific actions. To my knowledge, this was not done in connection with the April 1 adjustment. AMPI did submit a set of comments covering many of these points.

Mr. COELHO. Mr. Shaw is in the back of the room. Mr. Shaw, was a solicitation made for comments?

Mr. SHAW. No, sir.

Mr. COELHO. It was not. Is this the first time, Neal, in your opinion that that was done?

Mr. BJORNSON. It is the first time in my recollection that this has not been done.

Mr. COELHO. Let me ask you another question. It appears to me that at a time when this whole question, everything, is so controversial, I have a hard time understanding why the Department of Agriculture would do something that appears to be, on the face of it, obviously illegal. It may not be once we get into it, but it appears to be obviously illegal.

Do you feel that they knew that they were going over 50 cents when they started this? What is the reason? Neal, why don't you start off. What is the reason for it? Why are they doing what they are doing?

Mr. BJORNSON. We can speculate on it. I think if we look at it from the Department's standpoint, it is argued that we took two actions. One was the 50-cent price-support reduction. The other was a series of unrelated administrative actions——

Mr. COELHO. At the same time?

Mr. BJORNSON. At the same time, in calculating the purchase prices for the product. You cannot look at them, unfortunately, as unrelated because they do fit together. Jointly, they determine what the actual level of the announced reduction was.

Mr. COELHO. Was the announcement of both actions done at the same time?

Mr. BJORNSON. The announcement of the actions was made at the same time.

Mr. COELHO. Did they specify at the time that they were announced that they were separate actions and that one should not impact on the other?

Mr. BJORNSON. The announcement, as I recall, the announcement was phrased as a 50-cent price-support reduction and these other actions are also being taken. There was no attempt made to quantify the effect of the action.

Mr. COELHO. There was not an attempt at the time to say that there is a 50-cent price reduction and there will be further impact, but these are separate actions and so forth? They didn't say that?

Mr. BJORNSON. No.

Mr. ANDERSON. They did say, sir, that they were trying to adjust the marketplace to their view of what should occur.

Mr. COELHO. Say that again?

Mr. ANDERSON. The Secretary, as Mr. Gunderson pointed out earlier, said that the purpose behind the announcements and the changes in the announcement was to adjust the market so that there would be less incentive to sell to the Government. These were sticks that they sort of put into the nest to sort of push the little eaglets out to force them to fly.

Mr. COELHO. Well, as long as they are legal, they can force those eagles to fly, but it appears in this case, they let some eagles out of the cage that they shouldn't have. Now, we are going to try to go capture those eagles and maybe punish those who let them out of the cage.

Mr. Volkmer.

Mr. VOLKMER. Could I add to that also that the strategy was to change the type of CCC purchases that they were making?

Mr. ANDERSON. Yes, sir.

Mr. VOLKMER. Actually changes also in the manufacturing.

Mr. ANDERSON. Yes, sir. They are forcing the cheese industry into making 40-pound blocks when that isn't exactly the type of product that they would prefer to make. It is not commercial.

Mr. COELHO. And the reason that they don't want to make the 40 pound blocks?

Mr. ANDERSON. It is too expensive.

Mr. COELHO. OK. Does anybody else want to make any last minute comments?

Mr. TILLISON. I would just simply add that there is a tremendous danger in looking at averages. When you look at the USDA reports, you will see that yes, in fact, 70 percent of the whey solids are somehow recovered. However, you have to dig below averages. To me, I agree with the Congressmen when they say if you only have 80 whey plants and 678 cheese factories in the United States, how can you assume that all cheese factories are getting a 70-percent return on their whey? In addition to that, as Congressman Penny pointed out, it costs probably between 15 and 30 cents per hundredweight to dispose of the other 30 percent of the whey.

Mr. COELHO. Anybody else?

Mr. ANDERSON. We did have a meeting last week with our board of directors and some of the staff and the USDA were there. One of the most important things that we need to get across somehow, whether it is by legislation or just by USDA undersetting is that we need an early announcement of whatever it is they are going to do, the earlier the better, so that the commercial markets can begin to adjust to these downward adjustments ahead of time, and we can being to be back in there doing it commercially rather than letting the Government handle these problems.

Mr. COELHO. The Government probably prefers what is happening today. The uncertainty in the marketplace is advantageous to them, I assume.

Mr. ANDERSON. No; it hasn't been. They are buying much more product now than they had. That is what my testimony indicates, that the Government is now spending more. In an era when we are trying to cut the budget, we are now adopting policies that make it more expensive. That shouldn't be.

Mr. **Volkmer**. That is what I thought I was trying to bring out with Mr. Goldberg. The change in policy has brought about more costs as far as money costs.

Mr. **Coelho**. I appreciate the testimony of the panel very much. Thank you.

The next panel will be Tom Townsend, Paul Christ, and Jim Fraher. Tom, you may proceed.

STATEMENT OF THOMAS TOWNSEND, VICE PRESIDENT, MID-AMERICA DAIRYMEN, INC.

Mr. **Townsend**. Mr. Chairman, thank you.

I think really, first of all, I would ask that my printed statement be received for the record.

Mr. **Coelho**. Without objection, so ordered.

Mr. **Townsend**. It is always a pleasure to be here, Mr. Chairman. I am not sure I can add too much to what has already been said.

Mr. **Coelho**. As I said to an earlier witness, when you have sort of made your case, don't sell them the other way.

Mr. **Townsend**. I agree with that, Mr. Chairman.

I think basically the facts as far as cheese that I am testifying for today are that regardless of what you do about any of the rinky-dinky stuff, the facts are that the price of block cheese was reduced 6 cents per pound and converted to farm price at 61 cents. The price for barrel cheese was reduced 7.25 cents per pound, and that converts to about 74 cents at the farm level.

I think it really gets down to what you and Jim Jeffords said was the real issue, whether the USDA exceeded the authority that was granted under the law. I think in times past, we have looked at what the price support intent is. We have looked at it with every act since 1949. In the 1949 act and every subsequent act, USDA has consistently said that it is to set the price for milk for farmers.

I think that is the basic issue here today. Did, in fact, USDA establish a price support decrease of 50 cents per hundredweight consistent with law? I think the answer is clearly no, they did not. And I think that is a shame.

Whether you agree with the decision or the price level is immaterial at this point. It is the law, and whether you complied with the law or did not comply with the law or the intent of Congress is what is important.

With that, I will rest.

[The prepared statement of Mr. Townsend appears at the conclusion of the hearing.]

Mr. **Coelho**. Thank you, Tom. I think that is the reason that we have taken the action that we have. At a time when we are asking the dairy industry to absorb a budget cut of $500 million, at a time that we are forcing the industry to get united behind these type of budget cuts and reductions in their own program, we need at least to make sure that USDA protects the integrity of the program. If we can't do that, then there is no way that we as members of this subcommittee can urge the industry to do what needs to be done in order to cut the deficit and get this economy moving again.

So, I appreciate your comments, and I just want you to know that we intend to make sure that if it is a 50 cents cut that all of us can understand it. Obviously, we can't at this point, and I am not sure that anybody at USDA can or, at least, they are not advising us in a clearcut way.

Second, if it is over 50 cents, we intend to take the appropriate action, and I think that most people in this room understand what the appropriate action is.

Mr. Christ.

STATEMENT OF PAUL CHRIST, VICE PRESIDENT, PLANNING AND DAIRY ANALYSIS, LAND O'LAKES, INC.

Mr. CHRIST. Thank you, Mr. Chairman.

My name is Paul Christ. I am vice president for dairy planning and analysis at Land O'Lakes.

I would just like to cover some of the recommendations developed within the National Milk Producers Federation as a result of this development where the USDA adjustments in the price support program reflect a greater drop in ability to pay farmers than the 50 cents intended.

Our first recommendation is to restore the erroneous changes that were made. For example, we should reestablish the 3-cent, higher butter price on the east coast reflecting the situation before April 1. The 10-cent whey credit should be eliminated. The minus differential for barrel cheese should be restored to 3 cents, rather than 4.25. We also feel that the Department erred in making the adjustment between butter and nonfat dry milk. The federation recommended an even split between the two. We feel that this would have enhanced our ability to make commercial sales of butter without hurting our ability to make commercial sales of nonfat dry milk.

Now, the actions of the Secretary did reflect more than a 50-cent drop in ability to pay farmers. We would like to see this ability to pay restored immediately. However, if it is not restored immediately, when the price support adjustment for July 1 is considered, we feel that the remaining adjustment that would be made then should be limited to only 35 or 40 cents so that the total of the two adjustments amount to no more than $1. This was the intent of the law, and we think that as a last resort, this would be a way of fulfilling the intent of the law.

I want to make another point, and this is related to the general flim-flam associated with the price support actions over the last several years. That is the make allowance. We have argued for a number of years that there is a needed adjustment in make allowance in order that dairy processors are able to pay farmers the announced support price for milk. The difference between the purchase prices of products and the support price for milk is too small to cover all the costs of processing milk into those products.

We have repeatedly assembled data and provided it to the USDA to inform them as to what changes have taken place in the costs of processing. They have ignored these recommendations since October 1, 1980.

Recently, pay prices to farmers have been 40 to 55 cents below the announced support level when the product prices were at the support level.

So, we have, I guess, the Government saying one thing and, through their implementation actions, achieving another. If it is the intent of Congress and the Department of Agriculture to provide a lower level of support, let's be explicit about it, but let's provide a sufficient make allowance so that the plants competing in the industry can afford to pay the announced support price to farmers.

We are recommending that there would be a 30-cent increase in the make allowance for cheese manufacturing and a 40-cent increase in the make allowance for butter and nonfat dry milk processing.

This basically summarizes the recommendations, the outcome that we would like to see, of these hearings. We really appreciate your giving us the opportunity to present the information, and we thank you for your further efforts in this regard.

[The prepared statement of Mr. Christ appears at the conclusion of the hearing.]

Mr. COELHO. Thank you very much, Mr. Christ. We appreciate your cooperation as well.

Mr. Fraher.

STATEMENT OF JAMES FRAHER, ECONOMIST, INTER-STATE MILK PRODUCERS COOPERATIVE

Mr. FRAHER. Thank you, Mr. Chairman for this opportunity to make a statement on USDA's implementation of the April 1 price cut in the national support price for milk.

I am an economist with Inter-State Milk Producers Cooperative based in the Philadelphia market. We operate a major butter-powder plant at Mt. Holly Springs, PA.

We certainly concur with the testimony of previous witnesses that the effect of the actions taken by the Secretary on April 1 will be to reduce returns to our dairy farmer members considerably more than the intended 50-cent reduction in the support price. I also concur with the testimony of previous witnesses that the basic intent of the legislation was not followed and won't review with you, as I have in my prepared statement, the functioning of the support program and the specific actions taken effective April 1.

However, I would like to note that in my prepared statement, I have included two exhibits which show for the butter/nonfat dry milk combination and for cheese the impact of changes in the dairy price support program on the amount of money various types of dairy plant operators will have available to pay producers. I believe Neal Bjornson provided similar information. I would like to discuss briefly the table relating to butter and nonfat dry milk and make a few comments from our east coast perspective.

In the case of butter-powder plants located in the Northeast, such as our plant at Mt. Holly, our returns on milk going into butter and nonfat dry milk will be reduced by as much as 64 cents per hundredweight or 67 cents per hundredweight if the dry buttermilk impact is considered. What we are referring to here in the dry buttermilk impact is an effect that comes from lowering the prices for solids not fat or powder coming through on the buttermilk side, and those changes have resulted in a 6.25-cent reduction approximately in buttermilk solids prices which translates to a 3 cent per hundredweight reduction on the milk price. So, that is how we get the 67-cent reduction on a butter-powder plant in the East.

I note, too, that the reduction will have to be passed back to the dairy farmers.

The reason for the greater reduction in the Northeast, in addition, is associated with the elimination of the 3-cent higher purchase price for butter in the Northeast. The effect of doing away with the higher butter prices in the Northeast will primarily affect plant operators and producers in the Northeast. It will also have an adverse impact on plants located in the Midwest which regularly ship large quantities of butter to customers in the East.

For this butter shipped East, the plants will have to pay transportation costs of up to 4 cents per pound in order to compete with butter produced in the East, particularly during the heavy milk production season. The butter produced in the East does amount to approximately 10 percent of U.S. production.

As Paul Christ has indicated, we are therefore urging the Department to reconsider its action on butter purchase prices and restore the geographic differentials that existed prior to April 1.

Mr. Christ has also indicated that we are urging that the Department review changes in the support prices between butter and nonfat dry milk. We feel that further study needs to be done before we move away from the previous method of changing the support price where the drop in the support price was divided equally between butter and nonfat dry milk powder on the butter-powder side of the equation.

I thank you for the opportunity to testify today.

[The prepared statement of Mr. Frahar appears at the conclusion of the hearing.]

Mr. Coelho. Thank you very much. I appreciate all three of you testifying and coming here today. We will pursue this and, of course, we will keep you informed of what is happening.

The next panel is Jim Eichstadt, Tom Saunders, and Hal Hamilton.

STATEMENT OF JAMES EICHSTADT, DIRECTOR, COMMUNICATIONS, FARMERS UNION MILK MARKETING COOPERATIVE

Mr. Eichstadt. Mr. Chairman, I am James Eichstadt, director of communications for the Farmers Union Milk Marketing Cooperative based in Madison, WI. We represent 7,300 family dairy producers in the 7-State region of Wisconsin, Minnesota, Iowa, Illinois, Michigan, Nebraska, and South Dakota.

We commend you for calling a hearing on this subject so vital to the economic interests of our members, and we welcome this opportunity to speak out on these basic issues of the price support program at a time when far-reaching and harmful changes are being proposed.

I request that a copy of my formal statement be entered into the record. I will briefly summarize that statement.

Mr. Coelho. It will be made a part of the record.

Mr. Eichstadt. Thank you.

USDA's mismanagement of the dairy price support program in recent years has cost U.S. dairy producers over $2.3 billion in lost income and aggravated the dairy surplus problem. The April 1 price cut is just one part of a larger pattern of actions which have proved harmful to the average dairy producer and brought the current problems upon us.

Secretary Block acted illegally and arbitrarily in reducing the support price by 70 cents per hundredweight or more on April 1. This reduction above and beyond the 50-cent limit set by Congress will, according to the USDA data, cost the average Wisconsin dairy producer an added $1,093 per year in lost income with losses in other Midwest States averaging $861 in Minnesota, $1,189 in Michigan, $892 in Illinois, $692 in Iowa, $606 in Nebraska, and $564 in South Dakota.

Mr. Chairman, I must emphasize the importance of doing everything possible in the short time remaining to stop the next scheduled price cut on July 1 when, we fear, the Secretary will again overstep his authority. Your announcement of a formal investigation at this time is most welcome news.

Mr. Chairman, we have further evidence that USDA has consistently failed, since 1979, to maintain average manufacturing milk prices at the minimum levels set by Congress. The resulting gap between actual farm pay prices and the support price has cost the Nation's dairy farmers more than $2.3 billion in lost income from October 1979 to September 1984, with losses to the average Wisconsin dairy farmer running as high as $2,351 during the 1981-82 marketing year. This is an average figure, and we feel that the figure for the typical commercial dairy producer in Wisconsin is actually higher than that.

This income gap will worsen as the effects of the April 1 price cut reverberate throughout the farm economy. I want to add this portion of my statement now to the formal statement which I had earlier submitted to the committee, because it is new data we have arrived at.

Had the dairy program been properly administered, we may well not have the current surplus situation and the accompanying political pressures to dismantle a program which has worked well since its inception until the late 1970's. Low milk prices since that time have forced many producers to milk more cows to meet fixed operating expenses resulting in production which would not have occurred if farmers had only received the fair milk prices for them under the price support program. Thank you.

[The prepared statement of Mr. Eichstadt appears at the conclusion of the hearing.]

Mr. **COELHO**. Thank you.

Mr. Saunders, are you prepared?

Mr. **SAUNDERS**. I am prepared.

Mr. **COELHO**. Go right ahead.

STATEMENT OF TOM SAUNDERS, DAIRY FARMER, PRAIRIE FARM, WI

Mr. **Saunders**. I realize that my testimony today is not directed specifically at the investigation into the April 1 price cut, but it is directed at the situation out in the country.

Mr. **Coelho**. Well, Mr. Saunders, we have told everybody and we are firm in enforcing it that we are only going to hear about the April 1 price cut.

Mr. **Saunders**. Do you have a copy of my testimony?

Mr. **Coelho**. I have not seen your testimony, but that is all that we are going to listen to today, because that is what this hearing is all about. We have denied others that want to come in and discuss the farm bill. We are not listening to issues on the farm bill. We did that already once. We will do it some more, but this hearing is very specific.

Mr. **Saunders**. OK. Then, I would just simply say that what I heard earlier was that it was indicated that people weren't sure what the effect of the 50-cent price cut was. I would bring my testimony as a dairy farmer from Prairie Farm, WI.

The effect of the 50-cent price in April is devastating in the countryside. People are on the brink of foreclosure all over, and that does not only affect dairy farmers, but it affects rural business people and everyone.

If there is some questionable aspects to the April 50-cent price, for sure there should not be a 50-cent price cut in July.

[The prepared statement of Mr. Saunders appears at the conclusion of the hearing.]

Mr. **Coelho**. That is the point of our hearing, to find out if it was more than 50 cents. We feel that it is. Then, we want to take some corrective action before July 1 so that the Department knows what we are into.

Thank you, Mr. Saunders. We appreciate it. Your statement will be made a part of the official record so that we will have it.

Mr. Hamilton.

STATEMENT OF HAL HAMILTON, DAIRY FARMER, COMMUNITY FARM ALLIANCE OF KENTUCKY

Mr. **Hamilton**. Thank you.

I want to very briefly offer a dairy farmer's perspective on the April and July price cuts, not necessarily a perspective of the dairy industry.

Dairy farmers currently face the three following problems of crisis proportions: Insufficient income, surplus production, and a trend to concentration of production beyond optimal economies of scale. Legislation directed toward the future needs to be comprehensive and address all three problems.

Free market solutions are commonplace, especially in this town, and the April and July cuts are part of that mindless conventional wisdom. We are told that lower prices mean lower production. On an individual farm basis, this is obviously false. When my income per cow drops, I add cows.

In the aggregate, lowering prices drastically enough does bankrupt farmers, of course, but is this the dairy policy we want? It is time for our Nation to make a decision about agriculture. We can choose what David Stockman calls a dynamic economy, let the sharks eat the fishes, and eventually have a vertically integrated agriculture dominated by a few huge firms. Or, we can choose an agriculture of family scale farms sustained by Federal intervention.

Federal intervention to guarantee family scale production does not have to be expensive if we establish a system of quotas. Government purchase of surplus commodities benefits processors but costs taxpayers and hurts farmers.

Mr. COELHO. Mr. Hamilton, you have heard me tell others that we are only going to hear about the April 1 increase. On the farm bill, we would be glad to hear testimony at another time, but try to limit your comments to the April 1 increase, if you will, please.

Mr. HAMILTON. OK. In conclusion, we need higher prices and not lower prices, and we need mandatory supply management targeted to family scale farming. Farm policy should be constructed to serve farmers and should not be held hostage to those elements of the dairy industry that benefit from the flow of commodities into Government storage. Thank you.

[The prepared statement of Mr. Hamilton appears at the conclusion of the hearings.]

Mr. COELHO. Thank you, Mr. Hamilton. We have held hearings on the dairy bill, and we will hold more, but we are really trying to determine whether or not the Department exceeded its authority on this 50 cents, and that is the testimony we want to have today. But we appreciate your coming here, and we would be glad to have you back for other hearings on the general dairy bill.

We appreciate all three of you testifying.

I think what I will do before the next panel comes up is go over and vote and I will be right back.

[Recess taken.]

Mr. VOLKMER [acting chairman]. If the subcommittee will come to order, we will proceed and have our final panel. We have Mr. E. Linwood Tipton, executive vice president of the Milk Industry Foundation and International Association of Ice Cream Manufacturers and Mr. David Beren, economist and director of Milk Procurement, Southland Corp., Dallas, TX.

Mr. BEREN. Mr. Chairman, my name is David Beren. Mr. Tipton, unfortunately, was unable to stay. He had a prior engagement and a plane flight that he had to catch.

Mr. VOLKMER. All right. Mr. Tipton, I believe, has submitted a statement, and his statement will be made a part of the record. Mr. Beren, you may proceed with your statement or you may summarize, however you so desire.

[The prepared statement of Mr. Tipton appears at the conclusion of the hearing.]

STATEMENT OF DAVID A. BEREN, ECONOMIST AND DIRECTOR, MILK PROCUREMENT, SOUTHLAND CORP.

Mr. BEREN. Thank you, Mr. Chairman. My statement is about 5 minutes, so I will go ahead and present it.

I am David Beren with the Southland Corp. Southland markets dairy products throughout the United States. Our 21 plants produce a full line of dairy products, including fluid milks, ice cream, and cottage cheese. We service customers in all 50 States. We are also the world's largest operator of convenience stores, with 7,400 Seven-Eleven stores and 3,400 other retail outlets in the international division.

We believe that placing the entire impact of the 50-cent milk support price drop on nonfat dry milk, rather than splitting it between powder and butter, moved the dairy industry toward greater market orientation and decreased Government costs without any negative impact on farmers. We urge the Government to do this again on July 1.

The Southland Corp. supports the Dairy Support Program and endorses its continuation. We think the best way out of the current surplus is to increase demand. For that reason, we think that a shining star of the 1983 act was the promotion program.

Since the key to a stronger industry lies in demand, let's look in that direction to evaluate whether placing the entire April 1 support price drop on nonfat dry milk was more advisable than splitting it between butter and powder.

The primary purpose of the support reduction was to move supply and demand closer together. During a larger part of the last 12 months, butter prices were based upon actual market values, while powder continued to be supported above its real market worth. From June to early December 1984, butter prices were above the support level, reaching as much as 12 percent over supports.

As far as butter was concerned, the program has operated as it was intended to operate. That is, for 6 months, fat pricing was based on market values and when due to the historically flush fat availability which occurs in the winter when ice cream sales are low and fluid milk prices high, the support program undergridded the fat market, thus providing the support it is intended to provide.

Looking at nonfat dry milk, we see a very different story. The entire period since January 1984, nonfat dry milk prices rested on support. They were at all times within 1 cent of the 91-cent support price.

Government purchases of milk powder never ceased even while a tremendous shortage of milk existed in many markets. At times, we had to haul milk over 600 miles to meet consumer demand for dairy products in Texas, and milk had to be hauled all the way across the country from Wisconsin to Florida, while some organizations continued to sell nonfat dry milk to Uncle Sam. Throughout this period, no butter at all was sold to the Government.

The Government inventory of nonfat dry milk greatly exceeds that of butter. On the average, 100 pounds of cow's milk will produce 8.13 pounds of powder and 4.48 pounds of butter, a ratio of 1.8 to 1. However, Government inventories are 6 to 1.

The Commodity Credit Corporation currently has 971 million pounds of uncommitted powder and 154 million pounds of butter. In other words, the surplus of powder is three times greater than the surplus of butter on a milk equivalent basis.

We urge the U.S. Department of Agriculture again in July to take the entire reduction on nonfat dry milk and leave butter unchanged. Even with the lower powder support prices and stable supports, again in 1984 and 1985, we expect the commercial demand for fat from July through November to lift butter prices above the support level. When this occurs, Government butter purchases will cease. However, even at the reduced support level for nonfat dry milk, it is unlikely powder demand will be sufficient to raise its price above the floor level.

What if this prediction is wrong and lower nonfat dry milk price is below the market clearing level? That would be fine, because then what would happen is powder prices would rise above supports and the Government would cease purchasing powder, and the program would be functioning as it is supposed to, that is, buying during the flush and not buying during the short season.

The CCC buys proportionately more nonfat dry milk than butter. Therefore, lowering powder supports only and leaving butter unchanged decreases the cost of the support program, based on the amount of powder and butter purchased in fiscal year 1984, about $20 million.

One other point I would like to make is that total returns to dairy farmers are not affected by how the Government divides its support price reduction, because their product, raw milk, is made up of both skim milk and powder. In other words, we are discussing a method of reducing the costs of the Dairy Support Program without decreasing dairymen's income.

Thank you, Mr. Chairman, for this opportunity.

[The prepared statement of Mr. Beren appears at the conclusion of the hearing.]

Mr. VOLKMER. Thank you very much for your statement.

Some persons, including yours truly, have concerns that we may see more and more butter going to the CCC purchases as a result of the action of the USDA if they do exactly what you are talking about. You may see more butter stocks going into CCC.

Mr. BEREN. We anticipate something similar to what happened last year which is that sometime around July, the butter market, because of the fact that cream will be tight because of high ice cream sales, the butter market will go above the support level and butter sales will cease. This is what happened last year. It went on through December, through the first week in December. We expect this to happen again.

If you ended up getting less powder sales to the Government, I think that would be a good thing.

Mr. VOLKMER. That would probably also reflect, of course, in lower prices to the producer.

Mr. BEREN. I am sorry, I didn't understand.

Mr. VOLKMER. That is going to reflect in lower prices to the producer.

Mr. BEREN. A support price reduction would impact on the price to producers.

Mr. VOLKMER. Yes. Thank you very much. I have no further questions. I appreciate your testimony and your being here today.

Mr. COELHO. Thank you very much. I appreciate it. All the witnesses will have time to put anything additional in the record if they want. All members will have 5 legislative days to put additional material in the record.

We will pursue the investigations, reports, and so forth on the departmental action, and we will more than likely have another hearing substantially before July 1 to discuss that in greater detail.

This hearing is adjourned.

[Whereupon, at 3:37 p.m., the subcommittee recessed, to reconvene subject to the call of the Chair.]

[Material submitted for inclusion in the record follows:]

Statement by Richard Goldberg
Deputy Under Secretary for Agriculture
International Affairs and Commodity Programs
before the
House Committee on Agriculture
Subcommittee on Livestock, Dairy and Poultry
May 21, 1985

Mr. Chairman and Members of the Committee, I appreciate the opportunity to appear before you today to review the April 1 reduction in the national support price for milk. As you have requested, I will address both how the price cut was administered and the effect on purchases.

At the outset let me indicate that the April 1 reduction and the administrative actions which implemented the reduction are all set forth in the Final Regulatory Impact Analysis dated March 26, 1985. I respectfully request that a copy of that analysis be incorporated in the record with this statement.

The national support price for milk was reduced 50 cents per hundredweight (cwt.) on April 1 in accordance with the provisions of section 201(d) of the Agricultural Act of 1949 as added by the Dairy and Tobacco Adjustment Act of 1983. I welcome the opportunity to briefly address some of the administrative actions taken by the Secretary, and to simultaneously clear up any misunderstanding or misinformation which has spread through the dairy industry as a result.

At the outset, I would like to emphasize that the April 1 administrative actions taken were based on the best information available at the time the decisions were made. We believe that, as a package, they were in the best interests of not only the Commodity Credit Corporation (CCC) but the dairy industry and taxpayers as well. We further believe that these actions were clearly consistent with the objectives of:

-- Supporting the price of milk to farmers in accordance with legislative mandates;

-- Managing CCC inventories effectively and efficiently; and

-- Achieving cost savings without adversely affecting the price support objectives.

In announcing the decision on March 29, 1985, Secretary Block emphasized that the package of actions was an effort to reduce incentives for the dairy industry to sell dairy products to CCC as a primary market outlet. Since much debate in connection with the farm legislation which is currently under consideration will focus on surplus dairy products, CCC wants to ensure that government policy is not encouraging the excessive sales of such products to CCC. The role of CCC and the legislative mandate is to provide a price support to farmers that will assure an adequate supply of milk. There should be no question of the U.S. dairy industry's capacity to meet those requirements.

There are some other important considerations that underlie the administrative decisions which took effect on April 1. It must be remembered that the dairy support program is national in scope and, out of necessity, must be based on averages. Also, the industry has the capacity to shift quickly in response to economic factors from producing cheese to producing butter/nonfat dry milk (NDM) and vice versa from the available milk supply. Therefore, it is critical to maintain a balance between the support purchase prices for those products purchased by CCC.

Now, to briefly review the administrative changes which became effective April 1:

Manufacturing Allowances

Manufacturing allowances, or "make allowances", are designed to reflect annual average costs for manufacturing cheese and butter/nonfat dry milk (NDM).

Manufacturing allowances were continued at the previous levels of $1.22 per cwt. of milk for butter/NDM and $1.37 per cwt. of milk for cheese. Conclusive data were not available upon which to base any change in these allowances. Moreover, any increase in the allowances would have directly offset the effect of the lower support price.

The most reliable indication of the adequacy of the allowances has been the difference between the average U.S. manufacturing milk price and the support price when CCC is buying reasonable, but not excessive, quantities of all three dairy products.

During the first seven months (October 1984-April 1985) of this marketing year the average price received by farmers was exactly equal to the average support price during that period--a period during which CCC purchased over six billion pounds milk equivalent of dairy products. This fact suggests that CCC's current manufacturing allowances are set at reasonable levels.

We did not increase the manufacturing allowance and contrary to reports published in the dairy industry, we did not lower it.

CCC Sales Policy

The CCC dairy product sales policy of setting sell-back prices at 110 percent of the support purchase price was retained. It was recognized that processors would have on hand dairy products that were made from milk produced prior to April 1. Therefore, products that were produced before April 1 and graded and offered to CCC by April 15, were purchased by CCC at the older higher support price.

Concern has been expressed by the industry relating to inventory value losses due to the drop in support price. While this concern is understood, an inventory value reduction will necessarily follow a price support reduction. And, it should be noted, the impact can be converse. For example, in years past, when support prices were increasing--sometimes twice a year--the industry was the recipient of inventory value gains.

Price Differential Between Block and Barrel Cheese

The price differential which CCC pays between block and barrel cheese was increased from 3 cents per pound to 4.25 cents per pound. This change more accurately reflects current and historical market value differentials and could encourage some shift from purchases of barrel cheese to block cheese.

Some have complained about this change and have used barrel cheese as an example to suggest that CCC actually lowered the support price not by 50 cents per cwt., but by 60-70 cents/cwt. Some have stated that small barrel cheese plants have been disadvantaged. That may be true. However, it is not the mandate of CCC to provide a sole market for, or a profit for, any particular plant or group of plants. Furthermore, to select the price impact on a single product purchased by CCC as a measure of the overall net effect of a reduction in the price support level is not proper since the industry can adjust to any misalignment in price.

Single Nationwide Purchase Price Established for Butter

Prior to April 1, CCC announced only one purchase price for butter--at New York City (NYC). A price at any other location was a calculated adjustment, based on published freight rates, from the NYC price. Last year the Interstate Commerce Commission exempted rail transporation of dairy products from regulation--which eliminated the requirement to publish freight rates.

In the absence of published freight rates, the single-price system will be easier to administer than either the previous system or establishing a 3-price regional system. The CCC purchase price is now the same for all regions, and that practice is identical to the practice for the purchase programs for cheese and NDM.

Purchase Prices for Butter and NDM

The reduction in the support price for milk used in making butter and NDM was allocated totally to NDM.

In recent years, purchases of NDM have far exceeded, relative to their portions present in milk, purchases of butter. CCC has been purchasing 60-70 percent of total NDM produced in the U.S.

Last fall when markets tightened, butter prices increased to CCC sell-back levels while NDM prices remained at support levels--an indication that purchase prices for those products were misaligned.

Putting all of the decrease on NDM should lead to a net increase in commercial use of nonfat milk solids and a substantial reduction in CCC costs, as compared to allocating the decrease equally between NDM and butter.

Allowance for Value of Whey Solids Non-Fat Established in Calculating Cheese Purchase Prices

A net value of 2.5 cents per pound of whey solids was established based upon a 15 cent dried whey average price minus an estimated 12.5 cents per pound processing cost and an estimated 70-percent utilization rate. The resulting amount (about 1 cent per pound of cheese) was deducted from the purchase price which would otherwise have been established for cheese.

In FY 1984, the weekly market price for whey powder for Central States production area averaged 15.3 cents per pound. During the first 31 weeks of FY 1985 it has averaged 19.6 cents per pound.

Moisture Levels for Cheese Purchased by CCC

The maximum acceptable moisture levels of 38.5 percent for block cheese and 36.5 percent for barrel cheese were retained.

Also, no additional premiums will be paid for moisture content below 34 percent. This does not mean that CCC will not buy cheese with a moisture content below 34 percent--but only that CCC will pay no additional premium. All barrel cheese purchased by CCC is purchased at a premium over the announced price, as is much of the block cheese. This change should have little, if any, economic impact on cheese plants.

For CCC purposes, moisture levels in the ranges specified are consistent with proper inventory management.

Of the barrel cheese in inventory, about 1/10 of that purchased since July 1, 1984 was below 34 percent moisture.

Mr. Chairman, your letter specifically requested that I address the effect of the price cut on purchases.

It is premature to measure any long-term effect. However, as noted previously, CCC purchased at the old, higher price those products produced before April 1 if graded and offered prior to April 15.

Since April 1, CCC has purchased the following quantities of products compared with the same time periods in 1984:

	Butter	NDM	- - - - - - - - - Cheese	- - - - - - - - -			
			Total	Block	Barrels	Process	Mozzarella
	------------------------Million lbs.--------------------------------						
April 1-15							
1984	9.590	31.879	29.675	8.194	18.546	1.563	1.372
1985	17.881	43.655	44.414	12.574	27.251	2.269	2.320
April 16-30							
1984	10.973	39.187	28.816	4.656	22.226	1.934	-
1985	18.676	43.170	31.514	7.162	22.975	1.377	-
May 1-15							
1984	11.519	40.109	31.797	3.470	24.918	.855	2.554
1985	22.926	42.981	33.856	6.413	22.416	1.227	3.800

In conclusion, Mr. Chairman and Members of the Committee, I believe that the actions taken by Secretary Block on April 1 were sound, responsible actions for the good of both the American taxpayer and the dairy industry. We have had relatively few complaints about those actions. In fact, favorable comments which we have received, both publicly and privately, substantiate our April 1 decisions. The Departmenet believes the decisions were fair, equitable, and accurately reflect the statutory requirements mandated by Congress in the 1983 Dairy and Tobacco Adjustment Act.

Thank you, Mr. Chairman. I will be happy to respond to any questions that you and your members may have.

FINAL REGULATORY IMPACT ANALYSIS

Date: March 26, 1985
Agency: JSDA-Agricultural Stabilization and Conservation Service
Contact: Charles N. Shaw
USDA-ASCS
P.O. Box 2415
Washington, D.C. 20013
Phone: (202) 447-7601

I. Title. Support Program for Milk, 1984-85 Marketing Year.

II. Need for Action.

The Agricultural Act of 1949, as amended, requires that the price of milk to producers be supported at a level that will assure an adequate supply of milk, reflect changes in the cost of production, and assure a level of farm income to maintain productive capacity sufficient to meet future needs. However, the program became unbalanced in recent years, i.e., Commodity Credit Corporation (CCC) stocks of dairy products became burdensome, resulting in budgetary costs far in excess of those necessary to accomplish the program objectives. The Dairy and Tobacco Adjustment Act of 1983 (the 1983 Act) articulates the desire by Congress and the Administration to bring milk production into closer balance with commercial consumption, and to reduce the budgetary cost of the milk price support program. Thus, the goals of the 1983 Act are to encourage the adjustment of milk production to levels consistent with the national demand for milk and the products of milk.

The 1983 Act authorizes the Secretary to reduce the price support rate in effect on April 1, 1985, by 50 cents per hundredweight (cwt.) if the Secretary estimates that for the 12-month period beginning on that date net price support purchases of milk or the products of milk will be in excess of 6 billion pounds milk equivalent. The estimate contained in Appendix Table 1 of this analysis is net price support purchases of 9.1 billion pounds if the support price is lowered and 11.7 billion pounds if the support price is unchanged. Thus, even with the 50-cent reduction in support price, surplus purchases are estimated well above the trigger level set by the Congress. In addition, administrative program operations are reviewed periodically to determine if any changes are warranted.

III. Options Considered with Selected Options Designated.

A. Support Price Level.

1. Lower support price 50 cents per cwt. on April 1 to $12.10 per cwt. for milk containing 3.67-percent milkfat (Selected).

2. Leave support price unchanged on April 1 at $12.60 per cwt.

B. Administrative Program Operations.

1. Manufacturing Margins.

    a. Continue current manufacturing allowances of $1.22 per cwt. of milk for butter/nonfat dry milk (NDM) and $1.37 per cwt. of milk for cheese (Selected).

    b. Increase manufacturing allowances.

    c. Average current allowances and establish $1.30 per cwt. manufacturing allowance for milk used in butter/NDM and cheese.

2. CCC Sell-Back Policy.

    a. Maintain current CCC sales policy of adjusting sell-back prices to 110 percent of the new support purchase prices (Selected).

    b. Maintain current sell-back prices for 3 months following a downward price support adjustment.

    c. Continue current CCC sales policy except increase sell-back price of aged cheese to 115 percent of the new support purchase price.

3. Price Differential Between Block and Barrel Cheese.

    a. Continue current 3-cent per pound differential.

    b. Increase the differential to 4.25 cents per pound (Selected). Barrel cheese purchase prices would be set 4.25 cents per pound below block cheese purchase prices.

4. Pricing System for Butter Purchases.

    a. Continue the present butter pricing system.

    b. Establish a single, nationwide purchase price for butter (Selected).

    c. Establish a 3-price regional system for butter purchase prices.

5. Allocating Purchase Price Change Between Butter and NDM.

    a. Allocate entire share of support price reduction of butter/NDM to NDM (Selected).

    b. Allocate support price reduction of butter/NDM equally between butter and NDM.

6. Establishing a Value for Whey Solids-Not-Fat (S.N.F.) in Calculating Cheese Purchase Prices.

   a. Allocate a whey allowance value in calculating cheese prices based upon a projected net return of 5 cents per pound of whey S.N.F.

   b. Retain the current zero whey allowance in calculating cheese purchase prices.

   c. Allocate a whey allowance value in calculating cheese prices based upon a projected net return of 2.5 cents per pound of whey S.N.F. (Selected).

7. Establishing a Maximum and Minimum Moisture Level for Barrel Cheese Purchased by CCC.

   a. Continue current maximum acceptable moisture levels of 38.5 percent for block cheese and 36.5 percent for barrel cheese (Selected).

   b. Raise acceptable maximum moisture level for barrel cheese to the same level as for block cheese--38.5 percent.

   c. Continue to pay additional premiums on low moisture cheese with no minimum moisture cut-off level.

   d. Pay no additional premiums for cheese with a moisture content below 34 percent (Selected).

IV. Legislative Basis for Action.

Section 201(c) of the Agricultural Act of 1949 (the 1949 Act) provides that the price of milk shall be supported at a level not in excess of 90 percent nor less than 75 percent of parity as the Secretary determines necessary in order to assure an adequate supply of pure and wholesome milk to meet current needs, reflect changes in the cost of production, and assure a level of farm income adequate to maintain productive capacity sufficient to meet anticipated future needs.

Section 201(d) of the 1949 Act, as amended by the 1983 Act, also requires that for the period beginning with the first day of the first calendar month following the date of enactment of the 1983 Act and ending on March 31, 1985, to encourage the adjustment of milk production to levels consistent with the national demand for milk and the products of milk, the Secretary shall provide for a reduction of 50-cents per cwt. to be made in the price received on all milk produced in the United States and marketed by producers for commercial use.

Section 201(d) of the 1949 Act, as amended by the 1983 Act, also requires that the Secretary shall, not later than January 1, 1984, provide for a milk diversion program under which the Secretary shall offer to enter into a contract, at any time up to February 1, 1984, with any producer of milk in the United States for the purpose of reducing the quantity of milk marketed by the producer for commercial use during the 15-month period beginning on January 1, 1984.

Section 201(d) of the 1949 Act, as amended by the 1983 Act, also provides that notwithstanding any other provision of law, for the period beginning on the first day of the first calendar month following the date of enactment of the 1983 Act and ending on September 30, 1985, the price of milk shall be supported at $12.60 per cwt. for milk containing 3.67-percent milkfat. The 1983 Act further provides, however, that 1) on April 1, 1985, if the Secretary estimates that for the 12-month period beginning on such date net price support purchases of milk or the products of milk would be in excess of 6 billion pounds milk equivalent, the Secretary may reduce the price support rate by 50-cents per cwt., 2) on July 1, 1985, if the Secretary estimates that for the 12-month period beginning on such date net price support purchases of milk or milk products would be in excess of 5 billion pounds milk equivalent, the Secretary may reduce the price support rate by 50-cents per cwt., and 3) on July 1, 1985, if the Secretary estimates that for the 12-month period beginning on such date net price support purchases of milk or milk products would be 5 billion pounds milk equivalent or less, and if the Secretary determines it necessary in order to assure an adequate supply of pure and wholesome milk to meet current needs, the Secretary may increase the price support rate in effect on such date in an amount not less than 50-cents per cwt.

V. Expected Impacts. (Appendix Table 2)

A. Direct Impacts

1. Price Support Program.

The price of milk is supported by CCC through purchases of butter, cheese and NDM at prices calculated to enable plant operators to pay dairy farmers, on average, a price equal to the support price. The effectiveness of the program depends in part on competitiveness between manufacturers for available supplies of milk so that the average price received by farmers will equal the announced support price. At times of significant price support purchases, the CCC purchase prices for these products tend to become the floor for the market prices of such products. While this floor on products has been maintained, the average manufacturing-grade milk price received by farmers in recent years was below the announced support price because excessive supplies prevailed in the marketplace. However, manufacturing grade prices during the first 5 months of the 1984-85 marketing year have averaged 9 cents above the announced support price as manufacturers actively bid for reduced supplies of milk.

The price support program operates on a national basis. Milk easily flows across geographical and political boundaries. If milk prices move out of alignment, milk will shift to the market of greatest return. Dairy product manufacturing plants tend to be located near the areas of greatest milk production. Thus, at any given time, surplus milk from any area tends to move to areas or regions with the manufacturing capacity to absorb the excess supplies. The weekly editions of Dairy Market News published by AMS, United States Department of Agriculture (USDA) continually report this movement.

2. Analytical Procedures and Background.

The USDA, as a part of normal program operations, conducts ongoing analyses of supply, demand and price conditions and trends in the dairy industry. These analyses, conducted by several USDA agencies, are based on data collected from multiple sources by the various agencies. These analyses are subsequently coordinated through the USDA Interagency Commodity Estimates Committee for Dairy. This Committee, composed of senior analysts from 5 different agencies within the USDA, is charged with the responsibility for providing the official USDA estimates of supply, demand and price conditions in the dairy industry. Results of USDA analyses are reported periodically in the Dairy Outlook and Situation, and in the World Agricultural Supply and Demand Estimates.

In conducting the USDA analyses, the Committee routinely considers several factors influencing supply and demand for dairy products. Demand factors affecting commercial disappearance--both on a per capita and total basis--were last published in the March 1984 issue of Dairy Outlook and Situation. These factors include U.S. population, civilian employment, per capita disposable income, and retail price indexes. On the supply side, factors include milk cows on farms, milk cow replacements, milk production per cow, total milk production, average milk prices received by farmers, value per 100 pounds of dairy ration fed, milk-feed price relationships, milk cow replacement cost, grain and other concentrates fed to milk cows, dairy pasture feed conditions, hay prices and utility cow prices. These factors were last published in the December 1984 issue of Dairy Outlook and Situation.

The USDA also considers milk-concentrate relationships, reported most recently in the June 1984 issue of Dairy Outlook and Situation. These include the price of all milk sold to plants, ration value, cost of concentrate feed, milk-feed differences and returns over concentrate costs. In estimating these relationships, analysts utilize the most recent estimates of feed prices.

Milk-feed relationships and returns over concentrate costs are used as measures of the well-being of dairy farming as an industry. Data on these variables are readily available on a timely basis. Feed costs account for about half of total milk production costs. Feed cost projections are reported in the World Agricultural Supply and Demand Estimates, published periodically by the World Agricultural Outlook Board, USDA. These estimates take into account impacts resulting from programs such as the Payment-In-Kind (PIK) and other Departmental programs.

Historical data on many of these variables are contained in Appendix Table 3. The economic variables analyzed herein were derived from these sources unless otherwise noted.

Concentrate costs increased from year-earlier levels during 1983, and the first half of 1984. A part of the increase is attributable to the drought and the PIK Program of 1983. Since mid-1984, concentrate costs have trailed year-earlier levels. The milk-feed price ratio increased during the last half of 1984, exceeding year-earlier levels, and was comparable to levels experienced in 1981 and 1982.

An additional indicator of farmer well-being is reflected in production trends. A large body of economic literature suggests that when an enterprise is profitable, sustained production increases are likely to result. It is true in the short-run that production may increase to offset higher costs, but if such production is unprofitable or only marginally profitable, production increases will not be sustained. December 1983 marked the 56th consecutive month that milk production had exceeded year-earlier levels. Thus, the expansion period extended over 4 1/2 years--which strongly indicates that milk production was a relatively profitable farm enterprise.

Milk production declined in calendar 1984 coinciding with the milk diversion program. Production trailed year-earlier levels throughout 1984 and January 1985--but production in February 1985, on a daily average basis, was again above the year-earlier level. This suggests that the brief respite in 1984 may have only delayed continuation of the expansion trend.

Purchases of dairy products by the CCC constitute a valid measure of commercial supply-demand balance. CCC purchase data are reported to the industry on a weekly basis and provide consistency checks which are used in conducting the analyses. When prices are artificially set above market-clearing levels, the quantity produced will exceed the quantity demanded. The difference between the two quantities is absorbed by the CCC through purchases under the price support program for dairy products.

Milk price changes projected to result from a policy option under consideration are reflected through the supply-demand sectors by use of a supply response factor of 0.15 and a demand response factor of -0.30. This provides an estimated percentage change in quantity for a 1-percent change in price. These factors are still applicable for measuring differences between options. These factors have been used by USDA in previous studies--most notably in The Impact of Dairy Imports on the U.S. Dairy Industry, AER NO. 378, Economic Research Service, USDA, January 1975.

Section 201(d) of the 1949 Act, as amended by the 1983 Act, attempts to correct the imbalance between dairy supply and demand because excessively high prices under the Federal price support program had encouraged overproduction and retarded growth in commercial sales.

Appendix Table 3 presents data that illustrate the imbalance in the dairy industry. Throughout the early 1970's, the number of dairy farms declined, as did the number of farms in general. Cow numbers also declined as productivity per cow improved. The net effect was relative stability in dairy production. However, the Food and Agriculture Act of 1977 mandated a significant increase in the minimum CCC support price for milk and mandated a semiannual support price adjustment. This removed any discretion available to the Secretary to adjust prices downward to changing conditions and removed much of the uncertainty as to the future direction of milk prices. Persistent increases in dairy supports, in turn, motivated dairy producers to increase production--from 122.4 billion pounds in 1978-79 to 138.8 billion pounds only 4 years later. This production increase resulted not only from increased productivity per cow, but also from an increase in cow numbers. At the same time, commercial use increased at a much slower pace, basically in line with population growth, but retarded somewhat by the higher prices and weak economic conditions. As a result, CCC purchases increased from 1.1 billion pounds milk equivalent in 1978-79 to 13.8 billion pounds milk equivalent in 1981-82 to 16.6 billion in 1982-83. Uncommitted CCC inventories at the end of 1982-83 were a burdensome 17.0 billion pounds milk equivalent.

For the 1980-81 marketing year, the support price for manufacturing milk was announced at $13.10 per cwt., effective October 1, 1980. This level represented 80 percent of parity. The first step toward bringing supplies back into line with demand was legislation enacted on March 31, 1981. This legislation rescinded the scheduled April 1, 1981 adjustment, which was intended to reflect changes in the parity index in the previous 6 months. Therefore, the support price for the entire 1980-81 marketing year was maintained at $13.10 per cwt.

The provisions of the 1949 Act, as amended by the Omnibus Budget Reconciliation Act of 1981, required the Secretary of Agriculture to set the support level for milk at 75 percent of parity which was $13.49 per cwt. on October 1, 1981, the beginning of the 1981-82 marketing year. Special legislation returned the support price to $13.10 per cwt. on October 20, 1981, and the Agriculture and Food Act of 1981 made it permanent for the 1981-82 marketing year. Provisions of the 1949 Act, as amended by the Omnibus Budget Reconciliation Act of 1982, set the minimum support price at $13.10 per cwt. for the 1982-83 and 1983-84 marketing years. The 1983 Act, however, set the 1983-84 support level at $12.60 per cwt., effective December 1, 1983.

3. Current Domestic Developments.

Milk production through December 1983 continued to exceed year-earlier levels. Even with the 50-cent per cwt. deduction in place, which began April 16, 1983, and the second 50-cent per cwt. deduction which was effective September 1, 1983, milk cow numbers for the 1982-83 marketing year averaged 87,000 above the previous year's level. This indicates that, in general, dairy farmers had not yet received price signals strong enough to result in the removal of excess resources from dairying.

With the beginning of the milk diversion program on January 1, 1984, some farmers contracted to reduce marketings by a specified amount. Some participants reduced marketing through the sale of cows--while others reduced feeding levels, increased the use of milk on the farm or a combination of these and other management factors. In addition, the 50 cent per cwt. lower support price on December 1, 1983, the 50-cent per cwt. deduction, and higher feed prices early in 1984 led to reduced production by some farmers not participating in the milk diversion program. Consequently, in 1983-84 cow numbers averaged 157,000 below 1982-83 levels, while output per cow on a daily average basis declined for the first time since 1972-73.

With the end of the 50-cent per cwt. deduction and the milk diversion program half-way through marketing year 1984-85, cow numbers are expected to average about 79,000 below 1983-84, while productivity per cow will again increase.

Feed supplies remain adequate, with larger estimated carryover stocks and projected lower prices. Thus, even with lower milk prices, the milk-feed ratio in 1984-85 will likely average higher than in 1983-84.

Commercial use of dairy products increased sharply in 1983-84. The 3-percent gain occurred despite small increases in retail dairy product prices. Retail dairy prices relative to other prices in the economy were favorable to the consumer. In addition, an improving economy and lower unemployment also contributed.

Commercial use in 1984-85 will grow--but at a slower rate. October-December 1984 use was up only about 0.6 percent, with use for the year likely to be up about 1 percent.

Retail dairy product prices will continue to show modest increases in 1984-85. This, combined with the continued strong economy and the dairy promotion program, will lend strength to commercial use.

With higher milk production and lower commercial use, CCC net removals were 16.6 billion pounds milk equivalent for 1982-83, an increase of 2.8 billion pounds above 1981-82. Removals in 1983-84, dropped to 10.4 billion pounds--as milk marketings declined and commercial use increased sharply. Removals in the 1984-85 marketing year are currently estimated at 9.1 billion pounds if the support price is lowered as authorized in the 1983 Act and 10.2 billion pounds if the support price is held at $12.60 per cwt. Purchases through mid-March totaled about 4 billion pounds milk equivalent.

4. Supply-Demand-Price-Income Impacts.

Projections of production, commercial use, CCC purchases, effective farm prices and farm cash receipts are shown in Table 1 and Table 2. These tables reflect the 1984-85 supply, demand and price estimates for options A-1 and A-2 which were defined in Section III. There is a range around these estimates of ± 1 percent of milk production and of commercial use.

Table 1. Projections of Supply, Use, and Purchases, 1984-85

Marketing Year	Production	Commercial Use	CCC Purchases
	--------------------	billion lbs.	---------------
1979-80	127.7	119.2	8.2
1980-81	131.7	119.9	12.7
1981-82	134.7	121.7	13.8
1982-83	138.8	121.9	16.6
1983-84	136.8	126.0	10.4
1984-85 Options			
A-1 1/	137.0	127.1	9.1
A-2	137.6	126.6	10.2

1/ Latest estimate of the USDA Interagency Commodity Estimates Committee for Dairy, and published in March 11, 1985 issue of World Agricultural Supply and Demand Estimates.

Table 2. Estimated Farm Milk Price and Income, 1984-85

Marketing Year	Effective Price 1/	Farm Cash Receipts 2/
	$/cwt.	Million $
1979-80	12.76	16,050
1980-81	13.74	17,920
1981-82	13.62	18,190
1982-83	13.30	18,410 3/
1983-84	12.72	17,460 3/ 4/
1984-85 Options		
A-1	12.80	18,040 4/
A-2	13.17	18,620 4/

1/ Average price received by farmers for all milk (at the plant) after adjustment for 50-cent or $1.00 per cwt. deductions.

2/ From the sale of milk.

3/ Adjusted to reflect 50-cent and $1.00 per cwt. deductions.

4/ Receipts adjusted to reflect deduction and/or diversion payments.

The price support program operates on a National basis--not on a regional or individual producer basis. However, it principally affects dairy farm income in the areas of greatest milk production. Implementation of the new provisions will have the greatest effect in the same areas. More than 60 percent of the nation's milk production is concentrated in eight States: Wisconsin, California, New York, Minnesota, Pennsylvania, Michigan, Ohio and Iowa. However, every milk producer in the United States who markets milk commercially will be affected by the program.

Either price support option analyzed in this paper will result in profits for some dairy operations and losses for others. Individual producer costs vary widely depending on organization and efficiency of the operation. Since these differences exist, the price support program is not a suitable vehicle for trying to assure all dairy producers a profit, or to stabilize dairy farm numbers. Also, program objectives are not geared to individual farmers or regional production. As shown clearly in Appendix Table 3, dairy farm numbers declined even in the most favorable historical years.

Some dairy farmers will go out of business regardless of dairy policy. Agricultural Census data show that from 1978 to 1982 (a time of increased prices and production) the number of farms selling milk or dairy products declined by about 17,000. Some dairy farmers will go out of business under implementation of any of the options considered. A long-term trend, based on data reported annually by SRS-USDA, shows that the number of operations with milk cows has declined steadily, while the average number of cows per operation has increased each year (Appendix Table 3). Assuming a continued increase in cows per operation and an increase in milk per cow in 1984-85, it is estimated that there would be some 12,250 fewer operations with milk cows than in 1983-1984. With the support price lowered as authorized, an additional decline of some 800 operations with milk cows could be expected.

B. Indirect Impacts.

1. Excess Resources in Dairy Production and Processing/Manufacturing Sectors.

Changes in dairy farm income can impact on the farm economy and the overall general economy. Thus, agribusiness firms servicing the dairy industry and local economies likely will be affected by changes in dairy farm income. Farm cash receipts from dairying in 1982-83 slightly exceeded cash receipts in 1981-82. In 1983-84, farm cash receipts (including adjustment for deductions and diversion payments) from dairying totaled about $17.5 billion--down nearly $1 billion from the previous year.

During the 1983-84 marketing year, cash receipts were down partially because collections from the two 50-cent deductions (on marketings from September 1, 1983-November 30, 1983) and the 50-cent deduction implemented on December 1, 1983, exceeded payments under the milk diversion program. With this situation reversed in 1984-85 (diversion payments will exceed deductions collected), adjusted cash receipts will increase from 1983-84 levels and again exceed $18 billion.

In a previous impact analysis, dated December 27, 1983, USDA estimated that the milk price support program at $13.10 per cwt. maintained market prices at $3.00 to $5.00 per cwt. above the level producers initially would receive if no support program were in effect--at a cost to taxpayers in excess of $2 billion annually. This indicated that the support program was maintaining excessive resources engaged in milk and dairy product production--with CCC purchases equal to about 12 percent of total U.S. milk production.

In 1983-84 (with the 50-cent deduction, 50-cent lower support price and milk diversion program in place for a portion of the year) CCC purchases still totaled about 7.6 percent of U.S. milk production. In 1984-85, even with the lowest support price permissible by law, CCC purchases are estimated at 6.6 percent of production. This indicates that even following the diversion program, excess resources will still be engaged in milk and dairy product production. This, in part, is due to gains in productivity per cow. For example, milk production in February 1985 (the latest data available) on a daily average basis was 85 million pounds above February 1984. This was attained from 99,000 fewer cows--at the same support price level. Cow numbers have also increased from the most recent low point which occurred in July 1984, about half-way through the 15-month diversion program.

Pressures for increases in production continue to build. The large number of milk replacement heifers per 100 cows on January 1, 1985, was a record level for that date. Also, even larger productivity gains per cow in the future appear likely--as a result of continued genetic improvement and potential effects of other factors such as Bovine Growth Hormones.

Excess resources also exist in the dairy processing/manufacturing sectors. As supplies increased to a peak during the 1982-83 year, additional capacity was brought on line and/or upgraded to handle the surplus. Consequently, when supplies declined during 1983-84 (in part due to the diversion program) many cooperative and proprietary plants actively sought additional supplies of milk so as to continue to operate their manufacturing facilities at a desired capacity level. Competition for the reduced supplies increased and "give-up" charges increased in an effort to retain the available milk for manufacturing uses--or to receive remuneration for making supplies available for shipment for fluid uses.

The extent of any indirect impacts is unclear. However, basic economics would suggest that excess resources being used in dairy could yield greater social return if used in some other productive activity. However, these resources may remain in dairying as long as their returns exceed their salvage value. Tax money spent on the dairy price support program could be used to produce other goods or services, to help reduce the large Federal deficit, or these dollars--if not needed for Government activity--could be devoted to private sector investment with its beneficial employment and income effects. Moreover, while there could be short-term rigidities in adjusting resource use in dairying, there is no reason to believe that resources would not shift to other productive uses, providing additional employment and income benefits.

2. Potential Impact on Livestock and Poultry Producers.

At the outset of the milk diversion program in January 1984, a great concern existed as to the potential effect of the milk diversion program on livestock and poultry prices. Milk cow numbers in February 1985 averaged 10,811,000--down 331,000 from November 1983--the month the bill was signed. This decline occurred without lowering cattle and hog prices the way some expected. In fact, utility cow prices during calendar year 1984 averaged $39.81 per cwt., compared with the average of $39.35 per cwt. in 1983. Cow numbers in 1984-85 are expected to average only 78,000 below 1983-84 levels, even with the support price lowered. Lowering the support price will result in an estimated average of 45,000 fewer cows than if the $12.60 support price were retained. Thus, options considered in this analysis are expected to have little, if any, impact on livestock and poultry producers.

C. USDA and Other Outlays.

CCC outlays for marketing years 1979-80 through 1983-84 and for 1984-85 options are summarized in Table 3. Lowering the support price (Option A-1) will result in CCC net outlays some $200 million lower than if the support price were not lowered. However, since deductions exceeded diversion payments in 1983-84 and the reverse will occur in 1984-85, net outlays this year will exceed 1983-84 levels, even though the quantity of products purchased by CCC is expected to be lower.

Table 3.

CCC Outlays 1/, 1979-80 through 1983-84 and Estimated 1984-85 Options

Item	1979-80	1980-81	1981-82	1982-83	1983-84	1984-85 Options 4/	
						A-1	A-2
	Million Dollars						
Estimated CCC purchase cost	1,262	1,991	2,282	2,716	1,983	1,556	1,761
Net outlays 2/	1,011	1,894	2,182	2,782	2,000	1,666	1,871
Deductions	-	-	-	254	833	327	327
Diversion payments	-	-	-	-	335	602	602
Net outlays 3/	1,011	1,894	2,182	2,528	1,502	1,941	2,146

1/ For explanation of CCC outlays, see special article entitled "Costs of the Dairy Price Support Program", Dairy Outlook and Situation, June 1981, P. 33-35, ERS, USDA.

2/ Before deductions from producers and diversion payments to participating produce

3/ After deductions from producers and diversion payments to participating producer

4/ Additional savings in purchase costs and net outlays may be realized from some program operation options selected. These are discussed in Section D, and, if realized, would be in addition to differences shown in this table.

D. Reasons for Selection of Options.

In accordance with provisions of the 1983 Act, an estimate was made of net support purchases of milk or the products of milk for the 12-month period beginning April 1, 1985. The estimated surplus, even with the selected option of lowering the support price by 50 cents per cwt., was well above the trigger levels set by the Congress in the 1983 Act. In addition, a 50-cent per cwt. reduction in the support price likely will about be offset by the end of the 50-cent per cwt. deduction on March 31, 1985. Thus, if the support price were not reduced on April 1, it would, in effect, increase prices to farmers--sending the incorrect price signal to further increase production. No significant structural adjustment has occurred in the production sector as a result of the milk diversion program. Thus, productive capacity remains for additional increases in milk production.

Commercial use of milk and dairy products during the April 1985/March 1986 decision year likely will increase about 2 percent from the year-earlier level. If the support price were not lowered, the increase in use would be lower, leading to larger CCC purchases and increased CCC costs.

Administrative program operations are reviewed periodically to determine if any changes are warranted. Such changes may be necessary in order to implement the lower support price or to improve the effectiveness and/or efficiency of the price support program. A number of such options were selected following this review.

Manufacturing allowances will be continued at the current levels of $1.22 per cwt. of milk for butter/NDM and $1.37 for cheese. Conclusive data are not readily available upon which to base any change. Moreover, any increase in allowances would directly offset the effect of that corresponding portion of the lower support price.

The most reliable indication of the adequacy of the allowances has been the difference between the average U.S. manufacturing milk price and the support price when CCC is buying reasonable, but not excessive, quantities of all three dairy products. The U.S. manufacturing milk price averaged 40 cents below support in the 1980-81 marketing year, 46 cents below in the 1981-82 and 1982-83 marketing years and 22 cents below in the 1983-84 marketing year. These years were characterized by a heavy milk surplus resulting in excessive CCC purchases and lack of incentive for manufacturers to compete for the excess milk. Since September 1984, with production adjustments occurring under the paid diversion program, market prices have averaged 9 cents above support.

The dairy processing industry contends that the main reason manufacturing prices were under support in the early 1980's was because manufacturing allowances had not kept pace with increases in processing costs since 1979. However, some of these increases may have been offset by increases in efficiency and reduced costs resulting from economies of scale as the number of manufacturing plants declined, average size increased, and capacity was expanded.

It was also decided to maintain current CCC sales policy of adjusting sell-back prices to 110 percent of the new support purchase prices. Market prices are not expected to reach sell-back levels during the next several months, but if they did, this policy would provide the opportunity to more quickly reflect the reduction in purchase price at retail levels.

The price differential which CCC pays between block and barrel cheese prices was increased from 3 cents per pound to 4.25 cents per pound. This change will more accurately reflect actual market value differentials, could result in CCC estimated savings of $2.7

million during the April-September 1985 period, and could encourage some shift from purchases of barrel cheese to purchases of block cheese.

When CCC began purchasing barrel cheese under the price support program in 1977, the market price differential averaged about 4.5 cents per pound less than for block cheese. However, the announced support purchase price for barrels was set 3 cents per pound below the announced purchase price for block cheese to compensate cheese manufacturers for the added costs of converting to using fiber barrels and for other added costs for selling to the Government.

Now, seven years later, the market differential still averages about 4.0 to 4.5 cents per pound while CCC continues to pay only 3 cents per pound less for barrel cheese.

The industry should have had enough time to absorb any "start-up" or re-tooling costs involved in converting to packaging cheese in fiber barrels. In FY 1982, CCC purchased about twice as much cheese in the form of barrels as in blocks. In FY 1984, the proportion had risen to about 4 to 1.

The pricing system for butter purchases was changed to a single, nationwide purchase price for butter.

Presently, CCC announces only one purchase price for butter--at New York City (NYC). A price at any other location is calculated by deducting from the NYC price 80 percent of the lowest published freight rate in effect on October 1, the beginning of the marketing year. However, the price at any location is not less than CCC's purchase price for butter at NYC minus 3 cents per pound.

The Interstate Commerce Commission (ICC) issued a Notice of Final Rule on June 29, 1984, exempting all rail transportation of poultry, meat and dairy products from regulation--which means that the rail carriers will not be required to publish freight rates. This exemption, which became effective on July 30, will affect CCC's use of freight rate differentials for pricing butter purchased at various locations under the milk support program. In the absence of published freight rates, the single-price system will be easier to administer than either continuing the present system or establishing a 3-price regional system; the CCC purchase cost will be the same for all regions, and will make that procedure identical to the purchase programs for cheese and NDM.

In calculating the new purchase prices for butter and NDM the decrease in the support price for milk used in making these products was allocated totally to NDM.

In recent years purchases of NDM have far exceeded, relative to their portions present in milk, purchases of butter. CCC has been purchasing 60-70 percent of the total NDM produced in the U.S.

Substitution of whey, whey products and casein for NDM has also contributed to declining commercial use of NDM. Last fall when markets tightened, butter prices increased to CCC sell-back levels while NDM prices remained firmly at support levels--an indication that purchase prices for these products are misaligned.

Allocating the entire decrease to the purchase price for NDM should reduce CCC costs by an estimated $37.5 million for the remainder of this marketing year--from a reduction of 30 million pounds purchased and from an additional 3.1 cents per pound lower purchase price on the volume actually purchased.

A net value for whey S.N.F. was established in calculating cheese purchase prices. A net value of 2.5 cents per pound was established based upon an estimated 2.5-cent per pound net return (15 cent dried whey average price minus 12.5-cent per pound processing cost) and a 70-percent utilization rate.

The maximum acceptable moisture level for barrel cheese was retained at 36.5 percent compared with 38.5 percent for block cheese. Higher moisture increases the risk of deterioration for barrel cheese that must be stored for long periods. This action will continue to ensure quality maintenance for barrel cheese purchased by CCC.

A minimum moisture level of 34 percent was established, below which CCC will pay no additional premiums. This will result in a CCC cost savings on any acquisitions of cheese with moisture below 34 percent. It also will discourage unnecessary removal of whey in barrel cheese, and will be consistent with industry practice on block cheese.

NOTE: Public Comment Section is covered in the Federal Register entry.

APPROVED:

Everett Rank

Administrator,
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MAR
Date

Director,
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3/28/85
Date

Acting Assistant Secretary for Economics

3/28/85
Date

for Under Secretary for
International Affairs and Commodity Programs

Date

Appendix Table 1. Milk production, utilization, and CCC removals (April 1/March 31 Decision Year)

Item	Units	1978/79	1979/80	1980/81	1981/82	1982/83	1983/84	1984/85 1/	1985/86 2/	1985/86 3/
Milk production	Bil. lb.	121.5	124.8	129.7	133.5	136.5	139.4	135.1	137.8	139.2
Farm use	Bil. lb.	2.6	2.4	2.3	2.3	2.4	2.6	4.0	2.3	2.3
Marketings	Bil. lb.	118.9	122.4	127.4	131.2	134.1	136.8 4/	131.1	135.5	136.9
Beginning commercial stks	Bil. lb.	5.0 4/	4.9	5.6	5.9	5.2	5.2	5.3	4.8	4.8
Imports	Bil. lb.	2.2	2.3	2.1	2.3	2.7	2.6	2.8	2.9	2.9
Commercial supply	Bil. lb.	126.1	129.6	135.1	139.4	142.0	144.6	139.2	143.2	144.6
Commercial use	Bil. lb.	119.4	120.6	117.6	121.0	121.5 4/	123.7 4/	126.0	128.7	127.5
Ending commercial stocks	Bil. lb.	4.9	5.6	5.9	5.2	5.2	5.3	4.8	5.4	5.4
Total utilization	Bil. lb.	124.3	126.2	123.5	126.2	126.7	129.0	130.8	134.1	132.9
CCC net removals	Bil. lb.	1.8	3.4	11.6	13.2	15.3	15.6	8.4	9.1	11.7
Butter	Mil. lb.	68	111	359	372	390	384	190	205	270
Cheese	Mil. lb.	38	103	420	558	724	774	450	490	620
Nonfat dry milk	Mil. lb.	226	343	731	897	985	994	645	660	790
Evaporated milk	Mil. lb.	18	16	19	18	22	27	20	22	22
Number of cows	Thous.	10779	10731	10820	10934	11023	11064	10813	10785	10895
Milk per cow	Lb.	11274	11631	11985	12208	12385	12604	12494	12777	12777

1/ Partially estimated.
2/ Preliminary estimate, based upon implementing price support reductions authorized in the Dairy and Tobacco Adjustment Act of 1983, followed by $11.60 per cwt. support price continued throughout the decision period.
3/ Preliminary estimate, based upon $12.60 per cwt. support price continued throughout the decision period.
4/ Adjusted to round.

ASCS/CAD/3-12-85/WP#0356t(7)

Appendix Table 2. Milk Production, Utilization, and CCC Removals

Item	Unit	1982-83 1/	1983-84 2/	1984-85 3/	1984-85 4/
Support level	Per cwt.	$13.10	$13.10/$12.60	$12.60/$12.10/$11.60	$12.60
Deduction	Per cwt.	$.50/$1.00	$1.00/$.50	$.50/0	$.50/0
Milk production	Bil. lb.	138.8	136.8	137.0	137.6
Farm use	Bil. lb.	2.4	3.2	3.4	3.4
Marketings	Bil. lb.	136.4	133.6	133.6	134.2
Beginning commercial stocks	Bil. lb.	4.6	5.2	5.2	5.2
Imports	Bil. lb.	2.7	2.8	2.8	2.8
Commercial supply	Bil. lb.	143.6	141.5	141.6	142.2
Commercial use	Bil. lb.	121.9	126.0	127.1	126.6
Ending commercial stocks	Bil. lb.	5.2	5.2	5.4	5.4
Total Utilization	Bil. lb.	127.0	131.2	132.5	132.0
CCC net removals	Bil. lb.	16.6	10.4	9.1	10.2
Butter	Mil. lb.	410	239	210	240
Cheese	Mil. lb.	820	540	475	525
Nonfat dry milk	Mil. lb.	1,047	768	720	780
Evaporated milk	Mil. lb.	22	24	25	25
Estimated CCC purchase costs	Millions	$2,716	$1,983	$1,556	$1,761
Net outlays 5/	Millions	$2,782	$2,000	$1,666	$1,871
Industry Deduction	Millions	$254	$833	$327	$327
Diversion Payments	Millions	---	$335	$602	$602
Net CCC outlays 6/	Millions	$2,528	$1,502	$1,941	$2,146
Number of cows	Thousands	11,075	10,918	10,840	10,885
Milk per cow	Lb.	12,529	12,532	12,640	12,640
Prices Received By Farmers:					
Manufacturing grade	Per cwt.	$12.66	$12.41	$12.13	$12.50
All Milk sold to plants	Per cwt.	$13.58	$13.34	$13.20	$13.57
Effective price 7/	Per cwt.	$13.30	$12.72	$12.89	$13.17
Farm cash receipts 8/	Millions	$18,410	$17,460	$18,040	$18,620
Margin	Per cwt.	$13.99	$14.48	$15.07	$15.07
Retail value	Per cwt.	$27.56	$27.82	$28.27	$28.64
Retail cost	Millions	$33,600	$35,050	$35,930	$36,260

1/ $13.10 support, April 16, 1983, initial deduction and September 1, 1983 additional 50-cent deduction implemented. 2/ Two 50-cent deductions effective October and November 1983, followed by one 50-cent deduction effective December 1, 1983; $12.60 effective December 1, 1983. 3/ Projected; assuming 50-cent deduction through March 31, 1985, followed by $12.10 support price April 1, 1985, and $11.60 support price effective July 1, 1985. 4/ Projected; assuming 50-cent deduction through March 31, 1985 with $12.60 support price retained throughout the marketing year. 5/ Before deductions from and/or diversion payments to producers. 6/ After deductions and/or diversion payments. 7/ Price received by farmers after applicable deductions. 8/ Receipts adjusted to reflect deductions and/or diversion payments.

ASCS/CAD/3-12-85/WP#0109t

Appendix Table 3. Selected Dairy Data

Marketing Year 1/	Operations With Milk Cows 2/	Milk Cows On Farm	Cows Per Operation	Milk Per Cow	Total Milk Production	All Milk Sold To Plants	Dairy Feed 16% Protein	Milk/Feed Price Relationship	CPI Dairy	Commercial Disappearance	CCC Net Purchases	CCC Uncommitted Inventories
		3/	4/	3/	3/	5/	5/	6/	7/	8/	9/	10/
	number	thous.	number	lbs.	mil. lbs.	dol/cwt.	dol/ton	lbs.	1967=100	mil. lbs.	mil. lbs.	mil. lbs.
1969/70	647,860	12,050	18.6	9,673	116,529	5.68	73.3	1.55	110.6	108,981	5,595	1,917
1970/71	591,870	11,873	20.1	9,951	118,121	5.85	79.1	1.48	114.6	108,909	7,189	3,094
1971/72	539,350	11,733	21.8	10,244	120,163	6.01	77.8	1.54	116.7	111,814	5,967	2,342
1972/73	497,040	11,497	23.1	10,147	116,611	6.67	102.7	1.30	122.1	113,010	2,097	436
1973/74	470,240	11,255	23.9	10,251	115,337	8.40	131.8	1.27	148.8	113,037	1,145	365
1974/75	443,610	11,172	25.2	10,287	114,919	8.38	138.4	1.21	154.3	113,688	2,236	12
1975/76	416,160	11,048	26.5	10,775	119,032	9.70	138.6	1.40	167.0	115,850	161	0
1976/77	393,510	10,970	27.9	11,136	122,152	9.63	144.1	1.34	172.7	115,069	6,876	4,038
1977/78	369,210	10,833	29.3	11,231	121,637	10.23	134.9	1.52	181.3	118,597	3,230	4,517
1978/79	349,470	10,746	30.7	11,395	122,425	11.73	150.3	1.56	201.6	119,756	1,112	3,038
1979/80	334,180	10,769	32.2	11,809	127,715	12.76	168.2	1.52	222.4	119,231	8,158	7,438
1980/81	320,160	10,868	33.9	12,117	131,704	13.74	196.2	1.40	241.2	119,925	12,662	9,948
1981/82	307,920	10,988	35.7	12,260	134,719	13.62	179.4	1.52	246.4	121,670	13,840	16,468
1982/83	299,140	11,075	37.0	12,529	138,780	13.57 11/	180.2	1.51 12/	249.3	121,856	16,629	16,[illegible]
1983/84	285,740	10,918	38.2	12,532	136,754	13.34 13/	197.4	1.35 14/	251.4	126,022	10,350	12,856
1984/85 15/												
A-1	272,700	10,840	39.8	12,640	137,000	13.20 16/	184.0	1.44 17/	255.0	127,100	9,100	5,770
A-2	273,490	10,885	39.8	12,640	137,600	13.57 18/	184.0	1.47 19/	259.0	126,600	10,200	6,870

NOTE: See footnotes on next page.

Appendix Table 3. Footnotes

1/ October 1 to September 30.

2/ An operation is any place having one or more milk cows on hand during the calendar year. Sources: February issue 1984 of Milk Production; Milk: Final Estimates 1979-82, Milk: Final Estimates 1975-78, and Milk: Final Estimates 1970-74, SRS, USDA.

3/ Simple average of reported monthly numbers. Sources: February issue 1984 of Milk Production; Milk: Final Estimates 1979-82, Milk: Final Estimates 1975-78 and Milk: Final Estimates 1970-74, SRS, USDA.

4/ Computed by dividing number of milk cows by number of operations.

5/ Simple average of reported monthly prices. Source: Agricultural Prices Annual Summaries for 1975, 1976, 1977, 1978, 1979, 1980, 1981, 1982 and 1983; Agricultural Prices monthly Reports, 1984, SRS, USDA.

6/ Pounds of 16% dairy feed equal in value to one pound of milk. Computed by dividing all milk price by dairy feed 16% protein times 20.

7/ Simple average of reported monthly index. Source: CPI Detailed Report, Bureau of the Labor Statistics, Department of Labor.

8/ Sum of quarterly reported disappearance on a milk equivalent, fat basis. Source: Dairy Outlook and Situation, ERS, USDA.

9/ Purchases by CCC less sales for unrestricted use. Sum of monthly reported purchases milk equivalent fat basis. Source: Commodity Fact Sheet, 1984-1985 Dairy Program, ASCS, USDA.

10/ CCC inventories not committed for program use. Computed milk equivalent, end of year dairy product stocks. Source: Commodity Fact Sheet, 1982-83 Dairy Program, ASCS, USDA.

11/ $13.30 after adjustment for deductions.

12/ 1.48 pounds after adjustment for deductions.

13/ $12.72 after adjustment for deductions.

14/ 1.29 pounds after adjustment for deductions.

15/ Projected.

16/ $12.80 after adjustment for deductions.

17/ 1.39 pounds after adjustment for deductions.

18/ $13.17 after adjustment for deductions.

19/ 1.43 pounds after adjustment for deductions.

WP#0114t(2)

TESTIMONY ON APRIL 1, 1985 DAIRY PRICE SUPPORT CUT AND THE ANNOUNCED CCC PURCHASE PRICES

TO: House Agricultural Subcommittee on Livestock, Dairy and Poultry

By
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May 21, 1985

Thank you for inviting me to appear at this important hearing. There is indeed a great deal of concern by many in the dairy industry over the April 1, 1985, CCC purchase prices. Although the support price was reduced 50 cents per hundredweight, it has been charged that these new CCC purchase prices will in actuality result in more than a 50 cent reduction in farm milk prices. Some charge that farm milk prices will fall more than 70 cents per hundredweight, that is, more than 20 cents below the $12.10 April 1, 1985, support price. The more than 70 cents per hundredweight appears too strong. However, a reduction between 50 and 70 cents per hundredweight appears to be a valid charge. I will explain the bases for this conclusion, but first it may be useful to review the intent of the dairy price support program as authorized by the Agricultural Act of 1949.

In the Agricultural Act of 1949 and subsequent amendments to that act, Congress specified three major guidelines for the operation of the price support program. First, it provided for minimum and maximum levels at which farm milk prices were to be supported.

Second, the program authorized the Secretary of Agriculture to determine the specific price within the minimum and maximum price specified in the legislation. The objective of the support program is to support the price of milk at a level that will assure an adequate supply of milk.

Third, the legislature specified that the price would be supported through purchases of milk and milk products. Since milk is a bulky, perishable product, the Government cannot reasonably buy raw milk. Therefore, it purchases all the butter, nonfat dry milk and cheese offered by processors at announced prices. These purchase prices are set at levels designed to enable manufacturers of these dairy products to pay farmers the announced support price for milk in surplus production periods. It is the third guideline that this hearing is addressing. The announced April 1, 1985 CCC purchase prices fail to meet this guideline for the following reasons:

1. The "manufacturing (make) allowances" on margins to cover the costs of processing milk into butter-powder and cheese is used to calculate the CCC purchase prices. The make allowances have not been increased since 1979. With increases in plant operating costs since then (energy, labor, packaging) it may be difficult for some plants to pay the April 1, 1985, support price of $12.10.

2. The CCC purchase prices before and after April 1, 1985, and the decrease in terms of milk equivalent are:

	Before April 1st	After April 1st	Decrease	Decrease in Milk Equivalent (100 lbs)
Chicago Butter	$1.4325	$1.4325	0¢	0¢
Nonfat dry milk	$ .9100	$ .8475	-6.25¢	50.8¢
Cheese				
Barrels	$1.3175	$1.2450	-7.25¢	71.2¢
Blocks	$1.3475	$1.2875	- 6¢	60.6¢

The new CCC purchase prices for butter and nonfat dry milk appear to be in line with a 50 cent reduction in the support price. Nevertheless, there still is a concern with butter-powder. All of the 50 cent cut for a butter-powder was placed upon nonfat dry milk. This does not help butter's competition with oleomargarine. In addition, previously a CCC purchase price was determined both for Chicago and New York. The Chicago butter price was always 3 cents per pound less than the New York CCC butter purchase price to reflect differences in freight cost of butter from Chicago. As of April 1, 1985, the

New York butter price was decreased 3 cents per pound with no change in the Chicago price. As of April 1, 1985, the CCC purchase price for Chicago and New York butter is the same. Thus, there now exists one national CCC purchase price for butter of $1.4325 per pound. This puts Chicago butter at a competitive disadvantage to New York butter and could impact on farm milk prices in Wisconsin and Minnesota, major butter producing states.

3. As you can see, the concern over the April 1st CCC purchase prices lies mainly with cheese. With a yield of 10.1 pounds of cheese per 100 pounds of milk, one would expect a 50 cent drop in the support price would reduce the CCC purchase price on cheese by 50 cents ÷ 10.1 or 4.95 cents per pound. However, the decrease was 7.25 cents for barrel cheese and 6 cents for blocks.

The justification for the quarter drop in cheese purchase prices was based upon an assumed net return or profit in whey solids-not-fat. A value for the fat in whey has been used in calculating CCC purchase prices for cheese, but never before was a net value assumed on the solids-not-fat in whey. This is the key issue in this hearing.

A value of about 36 cents per hundredweight of milk used for cheese attributed to the fat in whey is valid. Fat in whey of about .25 pounds per 100 pounds of milk may readily be removed and used to make whey cream butter. Thus, .25 pounds x $1.4325 per pound of butter yields 36 cents per hundredweight. Thus, with a net return (profit) on the fat in whey of 36 cents per hundredweight, the CCC purchase price of cheese may be lowered accordingly and still enable the cheese plant selling to the CCC to pay farmers the support price. However, an assumed value of 10 cents per hundredweight of milk for whey solids-not-fat is questionable for the following reasons: There are 287 cheese plants in Wisconsin but only 11 dry whey plants. Only half of these are capable of making dry whey for human use which commands a price of about 15 cents per pound. In addition, the majority of the whey drying plants are owned and operated by barrel cheese plants that are capable of selling to the government. Even these operators indicate that the assumed net return of 2.5 cents per pound of dry whey is too high. (2.5 cents was figured assuming that 70% of the whey solids-not-fat is processed at a 2.5¢ per pound net return, 15¢ per pound day whey value minus 12.5¢ per pound processing cost).

Thus, the majority of the cheese plants, especially the smaller plants, are not receiving a net return (profit) from their whey, but may actually have a net cost of disposing of this whey. Thus, the assumed value of 10 cents per hundredweight of milk attributed to whey solids-not-fat in calculating the April 1, 1985, purchase price for cheese appears too high.

4. Another concern is the spread of 4.25 cents per pound between barrel and block cheese ($1.2875 - $1.245). In the past this spread has been 3 cents per pound. The spread of 4.25 cents may be too large and places barrel cheese plants at a disadvantage to blocks.

Although the spread between barrels and blocks has averaged 4.26 cents per pound on the National Cheese Exchange at Green Bay, Wisconsin, as indicated by USDA, this is not justification for a 4.25 cent spread. The cheese industry uses reusable steel barrels for cheese not sold to the CCC. The CCC, however, only purchases cheese in non-reusable fiber barrels. This adds to the cost of barrel cheese of about $5 per barrel, or about one cent per pound of cheese. Therefore, the spread between barrels and blocks appears to still be about 3 cents per pound and not the assumed 4.25 cents. As a result, barrel cheese appears to be at a price disadvantage to block cheese.

5. A fifth concern is that starting on April 1st CCC will no longer pay a premium for barrel cheese below 34% moisture. A typical cheese plant turns out barrel cheese between 32% and 32.5% moisture. Higher moisture cheese will age faster and break down faster. In addition, higher moisture cheese is likely to contain more free whey which is not desired by CCC. Thus, the 34%

moisture level is not as attractive to barrel cheese producers.

6. Sixth, with barrels at a disadvantage to blocks, barrel prices will be depressed and this will eventually lower block prices as plants either sell more barrels on the commercial market rather than to the CCC or shift from barrel to block production. Thus, all cheese prices may drift lower and so will the price on 100 pounds of milk utilized for cheese.

7. The claim that the April 1, 1985, CCC purchase prices will result in more than a 50 cent per hundredweight drop in farm milk prices is substantiated by what has actually happened to dairy product prices and farm milk prices since the April 1st announcement. (See Table Below)

April 1, 1985, CCC Purchase Prices Compared to Wholesale Dairy Product Prices

	CCC Purchase Price/lb.	Wholesale Price/lb.	Difference	Per cwt. Milk Equivalent Difference
Chicago Butter	$1.4325	$1.4050	-2.75¢	12.1¢
Cheese				
Barrels	$1.2550	$1.2350	-2.0¢	20.2¢
Blocks	$1.2875	$1.2600	-2.75¢	27.8¢

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[a] As of May 10, 1985

As can be clearly seen wholesale prices are well below the CCC purchase prices. The differences in the purchase prices and wholesale prices on a milk equivalent bases are 12.1 cents per hundredweight on milk utilized for butter 20.2 cents per hundredweight for barrel cheese, and 27.8 cents per hundredweight on block cheese.

The April Minnesota-Wisconsin Price Series for 3.5 percent fat test was $11.62 per hundredweight, a decline of 33 cents from March and 78 cents from January. The $11.62 M-W price is 20 cents below the April 1st support price of $11.82 for 3.5 percent fat test. Thus, in conclusion it appears quite clear that the April 1, 1985, announced CCC purchase prices have resulted in more than a 50 cents drop in farm milk prices.

Statement of the
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before the
Subcommittee on Livestock, Dairy & Poultry
of the
United States House of Representatives
May 21, 1985

I am Robert F. Anderson, Executive Director of the National Cheese Institute (NCI) and the American Butter Institute (ABI). The National Cheese Institute and the American Butter Institute are broadly representative of the nation's cheese and butter industries. Their members from coast to coast and border to border include independent, proprietary and cooperative manufacturers, as well as assemblers, packagers, wholesalers, distributors and marketers of these products. ABI and NCI members represent over 80 percent of the butter and cheese marketed in the United States. Most important, they represent 2 of the 3 products which are the subject of today's hearing -- the impact of the April 1 dairy support announcement on the NDM, butter and cheese industries.

First of all, two charts to help compare events in 1984 and 1985.

TABLE I

Comparison of 1984/85 Monthly CCC Purchases

1000 pounds

	BUTTER		CHEESE		NDM
	Bulk	Print	40#	500#	Total
Jan. 1984	51,995	9,255	12,620	43,882	76,219
Jan. 1985	41,772	8,180	3,694	27,844	58,802
Feb. 1984	39,378	7,796	7,479	32,389	63,978
Feb. 1985	36,401	8,180	9,430	32,445	54,872
Mar. 1984	25,432	2,727	7,719	34,675	65,095
Mar. 1985	26,416	7,758	14,690	43,922	63,906
Apr. 1984	17,759	2,804	8,370	40,773	71,067
Apr. 1985	23,695	6,912	18,396	45,498	72,856
May 1984	19,751	3,149	8,526	54,131	86,763
May 1985					
June 1984	2,670	345	9,810	49,568	72,348

TABLE II

Comparison of 1984/85 Weekly CCC Purchases

1000 pounds

	BUTTER		CHEESE		NDM
week ending	Bulk	Print	40#	500#	Total
3/9/84	7,484	730	2,301	7,561	16,161
3/8/85	7,745	1,767	3,014	8,245	15,221
3/16/84	5,732	499	1,061	8,707	15,292
3/15/85	7,484	2,650	4,089	11,157	13,369
3/23/84	5,779	538	2,039	8,156	13,168
3/22/85	6,272	1,843	3,476	12,797	15,573
3/30/84	5,213	691	2,111	9,566	15,793
3/29/85	4,915	1,498	4,111	11,723	19,742
4/6/84	4,967	499	1,708	8,271	15,285
4/5/85	6,804	2,035	4,154	9,347	21,230
4/13/84	3,856	296	2,007	10,275	16,595
4/12/85	3,972	1,498	4,975	13,786	15,405
4/20/84	3,819	499	2,338	9,482	15,788
4/19/85	6,013	1,651	7,469	12,451	19,866
4/27/84	3,185	1,498	1,767	10,230	18,822
4/26/85	6,905	1,728	1,798	9,914	16,355
5/4/84	4,914	1,882	1,171	9,974	20,043
5/3/85	7,584	1,920	2,582	9,821	21,434
5/10/84	3,182	269	1,433	10,147	16,031
5/9/85	9,901	2,151	2,467	9,915	19,123
5/17/84	5,534	384	2,001	12,301	17,595
5/16/85					
5/24/84	5,023	230	2,653	13,029	19,346
5/23/85					
5/31/84	3,028	422	1,819	11,195	18,320
5/30/85					

An analysis of these charts show sales of butter and cheese to CCC in April reversed the 1985 trend which had been one of reduced sales relative to 1984. For example, butter sales to CCC in April compared to April 1984 increased from 20,563,000 pounds to 30,607,000 pounds.

Cheese in 40# blocks and 500# barrels jumped from 49,143,000 pounds in 1984 to 63,894,000 pounds in 1985. Two-thirds of the increase was in the more expensive 40# block styles, reflecting the government actions taken April 1 to discourage sales of the less expensive bulk barrel cheese.

Interestingly there was very little year to year change in CCC purchases of nonfat dry milk (NDM) which increased slightly from 71,067,000 pounds to 72,856,000 pounds.

These facts indicate the government actions of April 1 have seriously disrupted the butter and cheese markets. In so doing the cost of the program to the government has escalated up instead of staying on the downward path established earlier in the year.

In April alone the government spent $14.4 million more to support butter than a year earlier. Compare this to the $1.5 million increase in NDM purchases from April '84 to April '85. It is difficult to imagine how a nearly $13 million increase between butter and NDM sales to the government is supposed to eventually reflect a $37.5 million reduction in CCC costs by the end of this marketing year. This "cost reduction" in NDM purchases was given in the USDA position paper which purports to justify the refusal to allocate a proportionate share of the support price decrease to butter.

Compare the events of April to January. In January 1985, under the former pricing structures, CCC purchased 11,298,000 pounds less butter then in January 1984 -- a savings to the government of approximately $16.2 million. Sales of NDM were also down and the government saved $15.8 million over January 1984.

It would seem a review of events and the facts to date would indicate the USDA made a serious error in judgement by allocating the entire reduction to NDM and none to butter.

The purpose of the dairy support program is to provide an adequate supply of whole milk. To carry out this program the government purchases certain dairy products if and when they become surplus by assigning to butter, NDM and cheddar cheese fair and equitable prices. The government should not attempt to manipulate the market to its own purposes and ignore the commercial market.

The April 1 actions regarding cheese are a classic example of government blundering into a market situation without taking into account the mechanics of that market.

Bulk cheese is made and packaged so it can be stored for future processing in an efficient and economical manner. One of the factors that insures this condition is a reasonably low moisture, the lower the better. The moisture content is self controlling because if the cheese does not have sufficient moisture it will not meet the desired top U.S. grade standards for flavor, body and texture.

Cheese evolved over the centuries as a practical way of storing milk solids for future use. It should be understood the pounds of cheese obtained from 100 pounds of milk decreases as the amount of moisture decreases. Further, the amount of solids in the cheese are the valuable constituents and industry charts have been developed to determine the value of a pound of cheese at various moisture levels. Taking the April 1 barrel cheese support price of $1.2450, the calculations are as follows:

-- 10.1 pounds of cheese at 39% moisture @ $1.2450 per pound equals $12.57 per 100 pounds of milk.

-- 9.4785 pounds of cheese at 35% moisture @ $1.3266 per pound equals $12.57 per 100 pounds of milk.

-- 9.1955 pounds of cheese at 33% moisture @ $1.3765 per pound equals $12.57 per 100 pounds of milk.

So, the purchase cost of cheese solids made from 100 pounds of milk is exactly the same regardless of moisture content. And the price paid for milk is the same. However, the April 1 limitation of 34% on moisture price adjustment is $1.3470. The value per 100 pounds of milk for 33% moisture cheese is now only $12.38. This is the same as a 19¢ per hundred reduction in the support price of milk, clearly not the intent of the law. The government should pay for what it gets -- no more, no less.

Even so, the handling costs to the government are increased as the moisture content of the cheese is increased. For example, if the moisture is increased just 2%, say from 33% to 35%, there will be an additional 11 pounds of water in each barrel. In a 112,000# carlot there will be 4 extra barrels to be packaged, handled, shipped, stored and finally processed.

This extra moisture limits the length of time the cheese may be stored. Recall, the lower the moisture the longer the cheese will maintain its quality.

And finally, when the carlot of 33% and carlot of 35% cheese are processed the pounds of process cheese resulting from either lot will be the same because the pounds of solids are the same.

The April 1 announcement, in a separate action, increased the price spread between barrel and block cheese from 3¢ to 4¼¢. For some time the ratio of barrel to block sales to CCC had been about 3 to 1. In April it dropped to roughly 2 to 1. The USDA signals were clearly heard. Now the government has more tonnage of expensive block cheese that may not store as well as barrel cheese and is more expensive to eventually process.

The most unfortunate aspect of this situation is the fact USDA evidently overlooked a National Cheese Exchange rule which requires the buyer to make payment of an additional $5 per barrel when the seller packages the cheese to meet government fiber barrel specifications, that is about 1¢ per pound. The announced USDA dictated 4¼¢ spread was excessive -- as the market place has shown. The original 3¢ spread was nearer to the true market value.

Whey is the liquid portion of milk remaining after the cheese is made. The more acid the whey has the less valuable the whey becomes commercially. Cheddar whey is an acid whey and it has minimal commercial utilization and value. The USDA, however, lumped the whey from all cheeses into one calculation and assumed a value that is not representative of cheddar cheese -- the product for which the support price is intended. We have surveyed our members and find the average value of cheddar whey over processing costs is not more than 1¢ per pound. The adjustment for cheddar whey should therefore be between zero to .03, not .10.

As I said to this committee last March, ABI and NCI are vitally concerned that the dairy support program be administered and conducted in such a manner as to promote stability in the dairy industry in the interest of the farmer, manufacturer and consumer. Our policy is to encourage the government to adopt a program which will bring about a supply and demand market within a five year period. To accomplish this the government and industry will have to work together more closely.

A supply and demand market will mean more commercial storage of product and less government product overhanging and depressing the market. This means, in the short run, less uncontrolled give-away butter and cheese and more exports to needy nations. In the long run, the government should work with industry to maintain the forces of supply and demand and not unilaterally make rules (such as, the barrel-block spread, whey allowance or moisture limitations) which would not be acceptable commercial practices. Nor should the government assign one-price to butter when the commercial market traditionally understands and works under a multiple pricing system.

Likewise, in a period of anticipated lower milk prices, the government should announce these changes as early as possible so the commercial market can make appropriate adjustments. We understand this may take legislative action to implement or possibly a better understanding of the problem by the USDA.

There is another adjustment in the dairy support program that should be implemented to encourage commercial rather than government storage of cheese. Because cheddar cheese must be stored for a period of time before it is ready for the commercial market there is a reluctance to commercially store cheese when the value of the cheese is to be reduced by government action. To safeguard the inventory value of commercially stored cheese the announced sell-back price of government-owned cheese should not be lowered for six months after an announcement which lowers cheese support prices.

In a separate but corollary action, we suggest that during the first six months of storage the sell-back price of CCC-owned cheese be 110% of the announced CCC purchase price, as it is for other dairy supported products. After six months storage there is added value to cheese so the sell-back price should be increased to 115% of the announced purchase price. Of course, in both instances, if the market price is higher it would apply.

Thank you for the opportunity to present the views of the American Butter Institute and the National Cheese Institute. I would be pleased to answer any questions you may have.

STATEMENT OF NEAL R. BJORNSON, ASSISTANT TO THE GENERAL MANAGER, ASSOCIATED MILK PRODUCERS, INC.

I am Neal R. Bjornson, Assistant to the General Manager of Associated Milk Producers, Inc. AMPI is a dairy cooperative marketing association headquartered in San Antonio, Texas. The cooperative's membership is comprised of more than 31,000 dairy farm families in 20 states.

We appreciate the concern expressed by the Committee in holding this hearing to examine the impacts of the price support reduction made April 1, 1985.

The Dairy and Tobacco Adjustment Act of 1983 authorized the Secretary of Agriculture to reduce the dairy price support level by 50 cents per hundredweight on April 1, 1985 if estimated Commodity Credit Corporation purchases over the next 12 months exceeded 6.0 billion pounds milk equivalent. A similar reduction is authorized on July 1, 1985 if the estimate of CCC purchases at that time exceeds 5.0 billion pounds milk equivalent over the next 12 months.

USDA analysis of the dairy situation prior to April 1 indicated that CCC purchases would be in excess of the 6.0 billion pound level. Accordingly, Secretary Block announced a $12.10 price support level effective April 1, 1985.

In commenting on the proposed April 1 price support action, AMPI recommended that the support level be maintained at the $12.60 level established December 1, 1983. This recommendation was based on the financial condition of dairy farmers and the risk presented in terms of maintaining adequate supplies of milk should a rapid reduction in milk production capacity take place.

USDA's report, THE CURRENT FINANCIAL CONDITION OF FARMERS AND FARM LENDERS, pointed out that the number of highly leveraged dairy farmers (those with 40 to 70 percent debt-to-asset ratios) increased by 60 percent between 1980 and 1984. Further, dairy farmers in this category represented 17.8 percent of all dairy farmers, substantially above the 11.1 percent for all farmers.

Dairy farmers classed as very highly leveraged (those with debt-to-asset ratios in excess of 70 percent) were reported to have increased by 295 percent from 1980 to 1984. Again, the proportion of dairy farmers included in this group was above that for all farmers, 8.7 percent as opposed to 6.6 percent. Overall, the USDA study determined that a continuation of the economic conditions faced in 1984 would substantially increase the number of family farms facing financial stress.

So far in 1985, the major changes in economic conditions facing the dairy farmer have included the reduction in the price support level, product markets demoralized in anticipation of April 1 and July 1 price support reductions and the end of the diversion program.

AMPI again recommends that the price support reduction authorized July 1 not be made.

In the face of the weak financial condition of dairy farmers at present, any action to further reduce the price support level must be questioned. The term "adequate supply" might appear to have little meaning until the adequacy of supply is actually threatened. Then, the rebuilding of productive capacity is a slow process accompanied by prices higher than necessary if the exodus of producers had been avoided to begin with. Avoiding such consequences is the basis of the Dairy Price Support Program. On that basis alone, we recommend that the price support level be maintained.

The price support level is achieved through CCC purchases of basic manufactured products--butter, nonfat dry milk and Cheddar cheese--of stated quality at announced price levels. In calculating these prices, a processing margin is added to the price support level and deductions are made to account for the value of by-products in the manufacturing process. If the proper processing margin is used and the by-product values accurately reflect yield and market conditions, a plant of average efficiency should obtain sufficient return from a hundred pounds of average test milk to meet processing costs and have sufficient funds to pay the farmer the announced price support level

While the Secretary's announcement of the price support level effective April 1, 1985 officially set the price support at $12.10, 50 cents below the value prevailing since December 1, 1983, several administrative actions taken in connection with calculation of the purchase prices increase the effective value of the reduction. Depending on the area of the country, the products produced and the strength of by-product markets the effective reduction ranges from 51 to 74 cents. These effects are detailed in Tables 1 and 2.

The cause of these variances range from the simple fact of "rounding down" to assumptions of market strength which, at this time, do not appear supportable. The following comments briefly on these items.

Whey credit: A credit of 10 cents per hundredweight of milk was included in the development of purchase prices for cheese. With a yield factor of 10.1 pounds of cheese from 100 pounds of milk, this reduces the purchase price by one cent per pound and the effective support level on milk used in cheese production by 10 cents per hundredweight if the whey market does not provide the expected 10 cent net return. This is currently not the case nor is it likely that this return can be expected between now and July 1.

Barrel-Block cheese price spread: In establishing purchase prices for cheese, the price spread between Cheddar cheese in 40 pound blocks and 500 pound barrels was increased from 3.0 to 4.25 cents per pound. The effect of this action was to reduce the effective price support on milk used in the production of barrel cheese by 13 cents.

The change was justified on that basis that this represents the normal commercial price spread and that the three cent spread was initially set to allow processors time to make needed changes in their operations.

The commercial market spread between barrel and block cheese varies considerably depending on market conditions. There is no constant pattern of a 4.25 cent price spread.

Market prices just prior to the recent announcement showed a spread as narrow as two cents.

Commercial practice is not fully indicative of the spread that should apply to CCC purchase prices. Barrel cheese sold to CCC is packed in non-returnable fiber drums. The normal commercial practice is shipment in returnable steel drums. The non-recoverable cost of the fiber drum must be reflected in the purchase price. The reduction in the spread between the two product prices eliminates the recovery.

There are other costs associated with sales of barrel cheese to CCC as compared to commercial sales. A recent plant survey by National Milk Producers Federation indicated that total costs when selling barrel cheese to CCC were 2.4 cents higher than costs associated with commercial sales.

Flat pricing of butter: Elimination of the freight rate differential previously reflected in the purchase price of butter at New York and that of butter at points west of New York has the effect of reducing the effective support price for milk made into butter-nonfat dry milk in the northeast by 13 cents. It also has implications beyond price support operations in that it removes the freight differential that has assisted movement of butter between midwest and eastern points. Now, when butter moves between these points, the difference represented by transportation costs must be made up by producers.

It is possible that this action can have the effect of discouraging movement of butter to meet commercial market needs in favor of sales to CCC. If the commercial market is not sufficiently above the CCC purchase price to at least cover shipping costs, sales to the government could present a better alternative.

Price spread between fortified and nonfortified nonfat dry milk: In establishing CCC purchase prices for nonfat dry milk, the price spread between nonfortified nonfat dry milk and fortified product was decreased by a quarter cent per pound. This effectively reduces the support level on milk used in production of the fortified product by an additional two cents per hundredweight.

Much of the nonfat dry milk used in food assistance programs is vitamin fortified. In the past, CCC has frequently had to resort to reprocessing nonfortified nonfat dry milk stocks to meet these needs. The reprocessing operation is more costly than the direct purchase of fortified nonfat dry milk.

Rounding: When questions of rounding whole or partial cents were presented in determining product purchase prices, prices were rounded down. This had the effect of reducing the effective support price by an additional cent.

In addition to the problems noted above, continuation of the processing allowance for milk made into butter-nonfat dry milk at $1.22 per hundredweight and $1.37 for cheese continues a policy that has been inadequate for some time. These allowances were established October 1, 1979. Since then there have been substantial increases in plant operating costs. A plant survey conducted by the National Milk Producers Federation earlier this year indicated that costs for butter-nonfat dry milk plants have increased an average of 45 percent since 1979. Cheese production costs have risen by 30 percent since that time. Our own plant operations bear out these cost increases. Based on these cost surveys, the processing margin for milk made into butter-nonfat dry milk should be increased by 40 cents per hundredweight and that for cheese raised by 30 cents.

Anticipation of the April 1 price support reduction caused substantial problems in the marketing of manufactured dairy products and reduced returns to farmers. Early statements by USDA officials made it clear that the authorized reduction would be made. In the hope of avoiding the devaluation of product inventory, persons in the trade reduced inventories to the lowest level possible. This reduced market prices and, beginning in mid-February, resulted in increased CCC purchases.

Some have suggested that the increased CCC purchases are indicative of increased milk production in anticipation of the end of the Milk Diversion Program. However, USDA reports that total production of butter, nonfat dry milk and American type cheese during January, February and March was below year earlier levels. USDA also reports that both commercial and government cold storage stocks of butter and American cheese were substantially below a year earlier on March 31, 1985.

Table 4 presents a rough attempt to estimate the increased CCC removals resulting from this situation. Comparing the volume of CCC purchases during the first calendar quarter of 1985 with USDA's estimate of total CCC purchases for the 1984-85 marketing year, we find that the purchases of butter and cheese during the quarter represent a substantially larger portion of the total anticipated for the year than has been the case in the past. Actually, looking at the reduced production and lower stocks, CCC purchases should have been lower during the quarter.

The actions taken in connection with the April 1 price support reduction effectively reduced the support level by more than the announced 50 cents. These actions have varying effects on producers depending on the products produced from their milk. In addition, continuation of the inadequate processing allowance means that returns to farmers will continue to be depressed below the announced price support level..

We urge immediate action to correct these inequities as well as increasing processing allowances to adequately reflect processing costs. Further, we recommend that the price support reduction authorized for July 1 not be made and that related actions which have the effect of depressing farm income be avoided.

(Tables follow:)

TABLE 1: Effect of the April 1, 1985 price support reduction on the ability to pay farmers for milk made into butter-nonfat dry milk.

	Prior to 4/1/85		After 4/1/85	
	Chicago	New York	Chicago	New York
VALUE OF PRODUCT:				
Nonfat dry milk				
Nonfortified	$7.40	$7.40	$6.89	$6.89
Fortified	7.50	7.50	6.97	6.97
Butter	6.42	6.55	6.42	6.42
Total				
Butter/nonfortified nonfat dry milk	13.82	13.95	13.31	13.31
Butter/fortified nonfat dry milk	13.92	14.05	13.39	13.39
LESS PROCESSING ALLOWANCE	1.22	1.22	1.22	1.22
Milk value: Funds available to pay farmers				
Butter/nonfortified nonfat dry milk	12.60	12.73	12.09	12.09
Butter/fortified nonfat dry milk	12.70	12.83	12.17	12.17
Reduction in funds available to pay farmers				
Butter/nonfortified nonfat dry milk			.51	.64
Butter/fortified nonfat dry milk			.53	.66

Nonfat dry milk: 8.13 pounds produced from 100 pounds average test milk times announced CCC purchase prices.

Butter: 4.48 pounds produced from 100 pounds average test milk times announced CCC purchase prices.

TABLE 2: Effect of the April 1, 1985 price support reduction on the ability to pay farmers for milk made into cheese.

	Prior to 4/1/85		After 4/1/85	
	Barrel	Block	Barrel	Block
VALUE OF CHEESE PRODUCED:	$13.31	$13.61	$12.57	$13.00
LESS PROCESSING ALLOWANCE	1.37	1.37	1.37	1.37
Value of milk in cheese	11.94	12.24	11.20	11.63
By-product credit				
Whey cream	.36	.36	.36	.36
Whey solids	-0-	-0-	-0-	-0-
Total milk value: Funds available to pay farmers				
If whey solids value recovered	12.30	12.60	11.66	12.09
If whey solids value not recovered	12.30	12.60	11.56	11.99
Reduction in funds available to pay farmers				
If whey solids value recovered			.64	.51
If whey solids value not recovered			.74	.61

Cheese: 10.1 pounds produced from 100 pounds average test milk times announced CCC purchase prices.

Whey cream: .25 pounds times CCC purchase price for butter (Chicago).

TABLE 3: CCC removals, January - March, 1980-85, compared with purchases for the entire marketing year.

YEAR	PRODUCT	JAN-MAR PURCHASES (mil. lbs)	ANNUAL PURCHASES (mil. lbs)	JAN-MAR AS PERCENT OF TOTAL
1984-85	Butter	130.5	210 (est.)	62
	Cheese	158.1	475 (est)	33
	Nonfat	180.9	720 (est)	25
1983-84	Butter	143.2	242	59
	Cheese	148.8	540	28
	Nonfat	205.3	768	27
1982-83	Butter	172.5	409	42
	Cheese	200.9	796	25
	Nonfat	271.7	1,041	26
1981-82	Butter	164.0	383	43
	Cheese	129.6	588	22
	Nonfat	235.0	954	25
1980-81	Butter	143.7	357	40
	Cheese	131.4	518	25
	Nonfat	189.6	787	24
1979-80	Butter	41.1	236	17
	Cheese	51.4	320	16
	Nonfat	93.1	592	16
WEIGHTED AVERAGE 1979-80 THROUGH 1983-84				
	Butter	132.8	325.4	41
	Cheese	132.4	552.4	24
	Nonfat	198.9	828.4	24

WISCONSIN CHEESE MAKERS ASSOCIATION

INTRODUCTION

The Wisconsin Cheese Makers Association represents 175 manufacturers and wholesalers of cheese and butter in twelve states. The WCMA believes that the formulation of the April 1st CCC purchase price for cheddar cheese and the adjustment made to the cheddar block - barrel differential have essentially lowered cheese prices to the point where the net effect on producers' pay prices will be more than the 50 cent reduction Congress intended.

We recognize that, historically, dairymen producing milk for manufacture into cheese have received less than the set support price for their milk during surplus periods. These lower prices resulted from the cheese market reflecting the excess availability of product offered to commercial markets.

We submit, however, that through their new calculation for the cheddar cheese purchase price, as well as the increased block-barrel spread, market forces have been circumvented by USDA policy.

THE WHEY CREDIT

In calculating the government's purchase price for block cheddar cheese, the USDA in the past has taken the milk support price, added to it a cost of production or 'make' allowance, deducted a return for butterfat sold as whey cream, and divided by a yield factor of 10.1 pounds of cheddar cheese per 100 pounds of milk with a 3.67 percent butterfat content.

This methodology was used when the Support Price was reduced in December of 1983 from $13.10 down to $12.60 and resulted in a drop in the cheese purchase price of 4.75 cents.

Had the same formula been followed in calculating the April 1, 1985, support price reduction from $12.60 to $12.10, the cheese price would have dropped from $1.3475 to $1.2975, five (5) cents.

The USDA, however, added another deduction for the net value of whey solids not fat of 10 cents per hundred weight of milk. This, when factored into the formula lowers the cheese price another 1 cent to the current CCC purchase price of $1.2875.

The key question is, do cheese plants actually get a net margin, selling price less costs, for their whey of 10 cents per hundredweight of milk that they can return to the dairyman. A member survey by the WCMA clearly indicates that the answer is clearly NO.

Based on a response by 35.3 percent of the 150 cheese manufacturing businesses that are members, 71.7 percent indicate they realize nothing from the whey produced during cheesemaking. 17.0 percent indicated they realize 1 to 5 cents per hundredweight. 1.9 percent realize 6 to 9 cents and only 9.4 percent net 10 cents or more.

Since Wisconsin has 293 cheese plants and only 31 whey processing plants, the results of the survey would appear to hold up for the population of plants in Wisconsin and very likely in the rest of the country as well with 678 cheese plants and only 80 whey plants.

While some might say that this whey factor only affects those plants selling to the government, those familiar with the industry and how the market works realize all cheese plants are impacted.

In the cheese industry there is a commodity market called the National Cheese Exchange. On this market both barrel and block cheddar cheese are traded. The entire cheese industry uses this market as the basis for selling and buying product. Cheeses other than cheddar are priced as so many cents over or under this market's block price.

More importantly, the National Cheese Exchange looks to the government purchase price as a measure of what their prices must be to move product from plants to commercial use versus government sales. When the government price moves down, the Exchange price moves down about the same amount.

Therefore, with the CCC cheese price reduced 6 cents because of the whey credit, the Exchange price and, therefore, the commercial market reflect that factor, and all cheese plants are impacted. Yet only 10 percent of the plants receive a sufficient return for their whey to pay out an amount even close to 10 cents per hundredweight of milk.

Another point about the use of the whey credit is that whey is the only factor in either the cheese or butter-powder calculations that is not supported by government purchases. Therefore, it is subject to the volatility of the commercial market as well as impacted by milk protein imports.

70 percent of the cheese plants do not derive any margin for their whey, it is a cost not an income factor. They are not able to maintain their milk pay prices because their cheese price has been lowered on the erroneous assumption that they do.

For these reasons, the WCMA urges the Congress to work for the immediate removal of this factor from the cheddar cheese support price calculation.

THE BARREL-BLOCK PRICE SPREAD

Observing a commodity market without knowing all the inner workings, rules and requirements of that market can lead one to make erroneous assumptions and decisions.

Such is the case in the USDA's decision to increase the price spread between 40 pound cheddar blocks and 500 pound cheddar barrels from 3 cents to 4.25 cents.

In their Impact Analysis, the USDA states that the market spread between blocks and barrels averages 4.0 to 4.5 cents per pound while the CCC pays only 3 cents per pound less for barrel cheese.

If one looks at industry trade publications they will note that a notation follows the assembly barrel prices that states the prices quoted are for barrels returned. The National Cheese Exchange price carries no such notation, but if one is aware of the rules of the Exchange, or if they would just call the Exchange's president, one would learn that the seller has the option of filling a transaction with either returnable steel barrels or USDA fiber barrels. When fiber barrels are sold, the seller bills the buyer the agreed market price PLUS $5.00 per barrel for the additional cost of the barrels.

Since a barrel contains approximately 500 pounds of cheese, the buyer of barrel cheese on the exchange is actually paying approximately one cent more per pound for cheese in fiber barrels than in the returnable steel barrels. Therefore, while the 1984 average spread between block and barrel cheese on the Exchange was 4.34 cents per pound in 1984, whenever fiber barrels were sold the actual spread was approximately one cent less.

Averages can be very misleading. While the Exchange barrel-block spread averaged 4.34 cents the 52 weeks of 1984, for 23 of those weeks the spread was 3.5 cents or less. For 33 of those weeks, the spread was 4 cents or less. For only two weeks did the spread go lower than 3.5 cents, but for 9 weeks the spread was over 5 cents. Removing these abberations results in an average of 3.97 cents. Factoring in the 1 cent the seller receives for fiber barrels clearly shows that the 3 cent spread should have been maintained.

Barrel cheesemakers put the cost of the USDA fiber barrels and liners at about 1.5 to 1.75 cents per pound and the total cost of making cheese for the government in this type of barrel at 1.75 to 2.25 cents per pound more than the steel barrels.

When commercial buyers tell cheesemakers to go to the government with their cheese, the barrel cheesemaker shifts from steel to fiber barrels. His production costs increase dramatically, as does the time frame in which he gets paid, and the possibility of total rejection of his product on technicalities.

While the WCMA applauds the USDA's desire to remove the incentives for those who would choose to sell to the government when commercial markets are available for their product, we feel that they have gone beyond removing incentives to creating disincentives with this change.

It is clear that the USDA did not have all the facts when they increased the block-barrel spread from 3 to 4.25 cents. The WCMA sincerely hopes that the USDA will acknowledge their error and reduce the spread back to the industry followed 3 cents.

THE MOISTURE PREMIUM MISTAKE

On April 1st, the USDA did something that will not only make it more difficult for makers to produce an acceptable product, but that we feel will increase the cost of the support program. That 'something' was to set a minimum moisture of 34 percent below which no moisture premiums will be paid.

The reason for this change given in the Final Impact Analysis by the USDA is, "This will result in a CCC cost savings on acquisitions of cheese with moisture below 34 percent."

This type of logic is indisputable. The government will save the amount of money it has been paying in moisture premiums below 34 percent. BUT, this high minimum moisture level will result in an increase in the amount of product purchased and therefore an increase in the cost of transportation and storage.

It will also result in a more unstable and less storable product, a fact that the USDA more or less recognizes in the Final Impact Analysis.

In the paragraph above that in which they announce the new minimum moisture, they reject raising the maximum moisture level allowed in barrels from 36.5 percent. "Higher moisture increases the risk of deterioration for barrel cheese that must be stored for long periods," is the way they put it. We submit that this is true by setting a minimum moisture level as high as 34 percent also.

A look at the numbers is very revealing. A simple fact is that the higher the moisture level in cheese, the more total pounds of product there is produced from 100 pounds of milk. For every one percentage point the amount of moisture is increased in cheddar cheese, the pounds of product yielded increases 1.4 percent.

For the period March 25th through March 29th, the CCC purchased 10,810,000 pounds of barrels cheese. Let's assume that that cheese was at 32.5 percent moisture.

- The price at 32.5 percent moisture is $1.3756 per pound.
- Total Cost - $14,870,236
- The price at 34.0 percent moisture is $1.3470 per pound.
- Total Cost - $14,561,070
- Apparent savings - $309,166

But, the simple fact of the matter is that cheesemakers will not make cheese below 34 percent moisture since there is no incentive to do so. They will shoot for 34 percent moisture which will increase the amount of total product the government purchases.

Let's now assume the cheese purchased for the above week was under the 34 percent minimum moisture. The increased moisture level in the cheese increases the amount of product yielded by 2.1 percent. Therefore 10,810,000 pounds of cheese at 32.5 percent moisture becomes 11,037,010 pounds at 34 percent moisture.

- The price at 34.0 percent moisture is $1.3470 per pound.
- Total cost - $1.3470 times 11,037,010 = $14,866,852
- Actual savings - $14,870,236 for 10,810,000 @ 32.5%
  -14,866,852 for 11,037,010 @ 34.0%

  $ 3,384 but have 227,010 more lbs.

As the above numbers clearly show, the outlay reduction is almost non-existant (0.023%) and the CCC has 227,010 more pounds of product to cope with. That's 445 more barrels to haul and store.

Through May 3rd the CCC has purchased 185,527,000 pounds of barrel cheese. A one percent increase in the moisture level on that amount of cheese would result in an increase in CCC stocks of 2.597 million pounds. That's over 5,000 more barrels to be hauled and stored. Which, by the way, would simply be water.

The WCMA firmly believes that setting a minimum moisture level was a mistake. The actual savings the government will realize on product purchased and stored will be negligible if there is any at all. The government will have a less stable product which will probably not holdup in long storage. The industry will probably not be willing to buy it back and it will be less suitable for manufacture into process cheese for various food programs.

SUMMARY

The farm milk price should be the result of what the commercial market is willing to pay for dairy products depending on the supply available. The support program provides a safety net that farm milk prices can't fall through. By putting in the whey factor and increasing the barrel - block price differential, the USDA has increased the elasticity of that net to stretch further below the support price than has occured in the past.

We believe the action taken by the USDA in establishing a return factor for whey in the CCC cheese price formula (which in fact doesn't exist for the vast majority of plants buying milk from producers) essentially lowers the pay price to producers of manufacturing grade milk more than the intended 50 cents.

When the increase in the barrel-block spread is factored in, the milk price drop increases still more as plants making cheese in barrels for the CCC lose an additional 1 cent per pound or approximately 10 cents per hundredweight.

Neither the whey factor nor the barrel-block differential increase can be justified when one looks closely at the cheese industry. A very small percentage of cheese plants see any return from their whey and the commercial market does, in fact, recognize the higher cost of putting cheese in fiber barrels.

The WCMA believes that it was the intent of Congress in the Dairy Stabilization Act of 1983 that the Support Price for milk was to be reduced to $12.60 on April 1 and $11.60 on July 1 if certain supply situations existed. The USDA, with it's actions, has surpassed the reductions Congress intended.

If you don't have the money, you can't pay it out. The USDA through its actions, not the market, has reduced the amount plants have available to pay producers. The Wisconsin Cheese Makers Association requests that Congress take the action necessary to remove the additional burdens the USDA has placed on cheesemakers and producers alike.

Respectfully submitted,
WISCONSIN CHEESE MAKERS ASSOCIATION

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The National Milk Producers Federation is a national farm commodity organization representing virtually all of the dairy farmer cooperatives and their dairy farmer members who serve this nation by producing and marketing milk in every state in the Union.

Since its inception in 1916, the Federation has actively participated in the development of dairy programs which are a part of a total system of agricultural law and policy which can appropriately be termed a national food policy.

The policies of the Federation are determined by its membership on a basis that assures participation from across the nation. The policy positions expressed by NMPF are thus the only nationwide expression of dairy farmers and their cooperatives on national public policy.

Before the

LIVESTOCK, DAIRY AND POULTRY SUBCOMMITTEE

of the

COMMITTEE ON AGRICULTURE

U. S. HOUSE OF REPRESENTATIVES

With respect to
the Impact of the April 1, 1985 Changes in the
Price Support Program and Recommendations

May 21, 1985

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Statement of Impact on Dairy Farmers of Recent Changes in the Dairy Price Support Program Particularly as Relates to the Butter-Nonfat Dairy Milk Industry.

My name is James Frahar. I am an Economist for Inter-State Milk Producers Cooperative, a dairy farmer cooperative association representing 3,100 dairy farmers in the Mid-Atlantic region. Inter-State Milk Producers Cooperative supplies milk for the fluid milk market in the Mid-Atlantic area and in addition is engaged in the processing of milk into a variety of dairy products including: butter, nonfat dry milk, condensed buttermilk, and a range of condensed milk products. We operate a large reserve milk supply balancing plant at Mt. Holly, Pennsylvania. Butter and nonfat dry milk are the primary products manufactured at this plant. The Secretary of Agriculture took action effective April 1, 1985 the intent of which was to reduce the dairy price support level from $12.60 to $12.10 per hundredweight of milk. The effect upon our dairy farmers will be considerably greater than the intended reduction of 50 cents per hundredweight.

I would like to review briefly with you the action taken by the Secretary of Agriculture for the purpose of reducing the price support level. As you know, the dairy price support program is carried out through the purchase of butter, nonfat dry milk and cheddar cheese at prices designed to reflect on the average a price to producers for manufacturing grade milk equivalent to the announced support level. In reducing the price support level, the Department of Agriculture must estimate changes in purchase prices necessary to reflect a given change in the price of manufacturing grade milk. For example, approximately 10 pounds of cheese can be obtained from 100 pounds of milk. This means that a decrease of one cent in the price of cheese translates into 10 cents less per hundred pounds of milk the dairy plant has available to pay to dairy farmers. Other things being equal, a reduction of 50 cents in the support price could be achieved through reducing the purchase price for cheese by 5 cents.

In the case of butter and nonfat dry milk, the Secretary must also decide upon the relative amount of adjustment to be made in the butter price and the nonfat dry milk price since these products are made jointly from milk—the butter being manufactured from the butterfat portion of the milk and nonfat dry milk being manufactured from the solids-not-fat or skim milk portion of the milk. Purchase prices may be altered in such a manner as to reduce the butter price enough to reflect the decrease, or so as to reduce the nonfat dry milk purchase price enough to reflect the entire decrease, or the decrease may be distributed in various ways between the two products.

In my testimony, I will concentrate on the impact of the recent dairy price support program changes butter-powder plant operators. The National Milk Producers Federation will present other witnesses to discuss the impact of the price support changes upon cheese plant operators and patrons and other segments of the dairy industry. On March 29, Secretary Block announced that in order to reduce the dairy price support level 50 cents per hundredweight of milk the following steps were being taken:

--the purchase price for butter would be set at $1.4325 per pound throughout the country. This left the purchase price the same for the midwest and West but had the effect of reducing purchase prices for butter in the Northeast by as much as 3 cents per pound.

—the purchase price of nonfortified nonfat dry milk was reduced by $.0625 per pound from $.9100 to $.8475

--the purchase price of 40-60 pound blocks of cheddar cheese was reduced $.0600 cents per pound from $1.3475 to $1.2875

The intent was to achieve the reduction in the price support level through reducing the purchase price for nonfat dry milk and cheese. In addition, certain other refinements were made in program operations including the following:

--the plus differential paid for fortified nonfat dry milk was reduced from 1.25 cents per pound to 1.0 cent per pound.

--the minus price differential for barrel cheese compared to blocks was increased from 3.0 cents per pound to 4.25 cents per pound.

--a whey credit equivalent to 10 cents per hundred pounds of milk was assumed by the Department of Agriculture in calculating the change in the purchase price for cheese necessary to achieve a 50 cent reduction in the price support level.

--the government will no longer pay a further moisture adjustment on cheese having a moisture content under 34 percent.

In my prepared statement, I have included two exhibits which show for the butter-nonfat dry milk combination, and for cheese, the impact of the changes in the dairy price support program upon the amount of money various types of dairy plant operators have available to pay back to producers. I will discuss briefly the table relating to butter-nonfat milk and the table relating to cheese will be discussed by another National Milk Producers Federation witness.

The table shows that butter-nonfat dry milk plant operators in the Midwest and West and most other areas other than the Northeast would realize a reduction of 51 cents per hundredweight. For those plants selling fortified nonfat dry milk to the government, returns would be reduced 2 cents per hundredweight more because of the 1/4 cent per pound reduction in the premium for fortified nonfat dry milk.

Another factor further influencing the amount of money available for distribution to dairy farmers is associated with the lower prices for dry buttermilk which have resulted from the 6.25 cent reduction in the nonfat dry milk price. We estimate that returns per hundred pounds of milk to be further reduced 3 cents per hundredweight of milk as a result of lower dry buttermilk prices.

In the case of butter-powder plants located in the Northeast such as our plant at Mt. Holly, our returns on milk going into butter-nonfat dry milk will be reduced by as much as 64 cents per hundredweight or 67 cents if the dry buttermilk impact is considered. This reduction will have to be passed back to our dairy farmer members.

The reason for the greater reduction in the Northeast is associated with the elimination of the 3 cent higher purchase price for butter in the Northeast. For any fortified nonfat dry milk we sell to the government, our returns could be further reduced by 2 cents per hundred pounds as a result of lowering the premium on the fortified product. The impact of the doing away with higher butter prices in the Northeast will primarily affect plant operators and producers in the East. It also will have an adverse impact on butter plants located in the Midwest who regularly ship large quantities of butter to customers in the East. For this butter shipped East, the plants will have to pay transportation costs of up to 4 cents per pound in order to compete with butter produced in the East, particularly during the heavy milk production season. Butter production in the area where the butter purchase price is being reduced is equal to approximately 10 percent of the total butter production.

We urge that the Department of Agriculture reconsider the recent action on butter purchase prices and restore the geographic differentials that existed on butter prior to the April 1 reduction.The differentials were well understood and accepted. For more than 30 years they recognized the geographic flow of product and permitted the recovery of transportation costs from Midwest to East. The elimination of differentials resulted in a major disruption to a commercial market that moves approximately 150 million pounds of butter from the Midwest to East.

The issue of how to distribute changes in support prices as between butter and nonfat dry milk is important and deserving of further study. USDA did not make a convincing case that placing all of the price decrease on nonfat dry milk would increase commercial use of dairy products and thus reduce government purchases. In fact, industry studies indicate that rather large decreases would be required in nonfat dry milk prices to reclaim customers from whey, whey blends, and other proteins. Another study done recently by the Federation indicates that lowering of butter prices tends to generate a larger increase in commercial sales due to its greater price elasticity. Previous studies had considered only the impact on nonfat dry milk sales or butter sales of reducing CCC purchase prices. However, if the impact of changing butterfat and nonfat solids prices on the ingredient costs of other dairy products are considered, indications are that a greater total response might have been realized by placing all the decrease on butter. However, until more definitive work is done as to how to distribute price support changes as between butter and nonfat dry milk, the National Milk Producers Federation favors equal division of any price changes among the two products. We urge the Department to give much more analysis and consideration to splitting future adjustments than they apparently gave to the April 1 adjustment.

Statement of Impact on Dairy Farmers of Recent Changes in the Dairy Price Support Program as it Relates to the Cheese Industry

May 21, 1985

My name is Thomas Townsend. I am a Corporate Senior Vice-President of Mid-America Dairymen Inc., a dairy marketing cooperative representing 11,000 dairy farmers located in eleven states in the Central part of the United States. Mid-America Dairymen operates 28 major manufacturing plants which process milk into various dairy products including yogurt, whipped cream, half and half, cottage cheese, cheddar cheese, butter-nonfat dry milk and specialty dehydrated products.

I would like to discuss further the changes made in the the dairy price support program which became effective April 1, 1985. As previously indicated, the intent of these changes was to reduce the price support level by 50 cents per hundredweight. The effect upon many of our dairy farmers was much greater than the intended 50 cent reduction. The previous witness from National Milk Producers concentrated his testimony on the impact of the price support changes on dairy farmers supplying butter-nonfat dry milk plants. My testimony will relate to the impact upon cheese plant operators and dairy farmers supplying cheese plants. The impact of the April 1 price support change differ as between plants producing barrel cheese and 40-60 pound blocks. For plants who are making barrel cheese, the reduction in returns available for payment to dairy farmers is not 50 cents, but 74 cents. For plants making block cheddar cheese the reduction in return is 60 cents rather than the intended 50 cents. The additional 24 cent or 10 cent reduction to cheese plants is associated with one or both of the following two factors:

1. The 10 cent credit on whey which has the effect of reducing returns by 10 cents unless offset by increased returns from whey.

2. The widening of the minus differential on barrel cheese by 1.25 cents per pound from 3.0 to 4.25 cents. In terms of a hundred pounds of milk, this translates into a 13 cent reduction in returns available to pay to dairy farmers.

It is appropriate to give consideration to returns from whey in calculating purchase prices necessary to achieve a given level of price support. At times whey prices have been high enough to return additional money to dairy farmers. The calculation of a whey credit is further complicated by the fact that relatively few cheese plants have their own whey drying facilities. Many plant operators must transport liquid whey to a drying facility. In some cases, the whey must be disposed of in other ways and may represent an item of cost rather than a source of additional returns.

The Department of Agriculture calculated the 10 cent whey credit on the basis of the assumption that whey prices would average about 15 cents per pound during the April-October period and that average costs of processing whey are 12.5 cents per pound and that 70% of the liquid whey is processed.

It is our opinion that the market value of dry whey during the coming year is not likely to exceed, on average, the cost of handling and drying liquid whey. A review by National Milk Producers Federation's members indicate that whey processing costs for the past year indicated their average cost was between $.12 and $.13 per pound. In addition, some members reported that the cost of moving whey, some of which has to be moved in liquid form before concentrating, could amount to an additional four to six cents per pound of dry whey.

The market price for edible dry whey was recently in the $.125-.135 range. However, as we move into the flush production months, cheese production will increase as well as dry whey production. This likely could reduce the dry whey price to as little as $.12 per pound during the high production months. Milk production is recovering after the diversion program and we expect cheese production for the year to be above last year's levels. This will have a price-depressing effect on whey prices. Also, with reduced prices for nonfat dry milk this year, additional pressures on dry whey prices are likely. For the coming year, it is our estimate that the market price of dry whey will average near, or slightly below the cost of handling and processing it.

We urge the Department to restore the zero whey credit on whey.

The Department of Agriculture has, until the recent price support action, maintained a 3 cent minus differential on barrel cheese below the price of 40-60 pound block cheese since they began purchasing barrel cheese in 1977. The change to 4.25 cents was made in light of the significant increase in the proportion of barrel cheese purchased relative to block cheese and was justified on the basis that 4.25 cents is more reflective of market differentials.

The government also indicated that the significant increase in the purchases of barrel cheese was an indication that the three cent differential had encouraged the expansion of barrel cheese processing facilities. Preliminary results of a survey of packaging facilities at the plants of four members indicate that generally the expansion has been greater in block cheese than in barrels.

The reason for increased purchases of barrel cheese under the Price Support Program is related to the distribution of free cheese under assistance programs. The Department of Agriculture recognized this in a special article in the June, 1983 "Dairy Outlook and Situation" report.

A survey of six cooperatives who are members of National Milk Producers Federation and who produce both block and barrel cheese, showed that on the average, the additional packaging costs of selling barrel cheese to the government were 1.56 cents per pound higher than the cost of selling blocks. This indicates that the commercial market differential between barrels and blocks is not a reasonable basis for judging what the differential should be. If the commercial market, differential is used as a basis, adjustment should be made for the higher packaging costs associated with selling barrel cheese to the government.

We urge the Department to return to the 3.0 cent differential between barrel and block cheese which prevailed prior to April 1.

Statement of Impact on Dairy Farmers of Recent Changes in the Dairy Price Support Program

My name is Paul Christ. I am Vice-President, Planning and Dairy Analysis, of Land O' Lakes, Inc. Land O'Lakes has 6500 direct dairy farmer members and about 60 dairy cooperative members, representing another 15,000 dairy farmers. Purchasing milk, processing and marketing dairy products account for about $1.2 billion in business for Land O'Lakes. We operate 24 dairy processing plants in Minnesota, North Dakota, South Dakota and Wisconsin. These plants process milk into fluid milk, ice cream, cheese, butter, nonfat dry milk and whey powder. Land O'Lakes Food Division further processes many of these dairy products an markets more than 600 packaged food products.

The two previous witnesses for National Milk Producers Federation discussed the impact of the April 1 dairy price support action upon the ability of butter nonfat dry plant operators and cheese plant operators to pay dairy farmers. I would like to summarize what they have said, particularly as relates to further actions what may be taken under the dairy price support program.

Also, I would like to discuss several other matters which are of interest and importance relative to the operation of the dairy price support program and its impact on the nation's dairy farmers.

Our previous witnesses pointed out that the ability of butter nonfat dry milk plant operators to pay producers in the Eastern part of the country had been reduced as much ~~as~~ 67-69 cents per hundredweight instead of the intended 50 cents; and that Midwest plant operators shipping butter to commercial customers on the East coast were adversely affected by the elimination of this traditional differential for transportation. It was also pointed out that proceeds available to cheese plant operators to pay to dairy farmers were reduced 60 to 74 cents per hundredweight instead of the intended 50 cents because of the 10 cent whey credit and the reduction of 1.25 cents in the differential between barrel cheese and block cheese.

The previous witnesses made the following recommendations on behalf of their organization and the National Milk Producers Federation:

1. The butter pricing structure which provided up to a three cent higher price for butter in the East should be reestablished as it existed prior to April 1.
2. The 10 cent whey credit should be eliminated and the zero credit reestablished.
3. The minus differential for barrel cheese relative to 40-60 pound blocks should be returned to 3.0 cents from 4.25 cents.
4. Additional study is needed on the distribution of price support increases or decreases as between purchase prices for butter and nonfat dry milk. In the meantime, National Milk Producers Federation supports equal weighting between the two products.

It is our desire and recommendation that change be made immediately by USDA with respect to these matters.

On May 10, the National Milk Producers Federation Board passed a resolution requesting the Secretary to not further reduce the price on July 1, 1985 (see Exhibit 3). Frequent price adjustments are unstabilizing to the commercial market and the impact on dairy farmers will be unduly harsh while we are working with the Congress to construct a workable dairy program. However, in the event the Secretary sees fit to reduce the price again on July 1, it is important that the changes which we have recommended be made at that time. Since the changes made April 1 in most cases have reduced returns to producers by more than the intended 50 cents this should be recognized and any further decreases should not exceed the amount prescribed by law for the April 1 and July 1 period combined.

The action taken by the Secretary of Agriculture on April 1 had the effect of reducing returns 60-65 cents per hundredweight, 10-15 cents more than intended by Congress. The combined total reduction on April 1 and July 1 was intended to not exceed $1.00. Therefore, if the Secretary does not change the April 1 adjustment, as we recommend, he has only 35-40 cents adjustment left to make to achieve the $1.00 total.

A matter of great importance with respect to carrying out the price support program is the application of appropriate make allowances in order to calculate purchase prices at levels adequate to permit dairy plant operators to pay dairy farmers on the average at least the announced price support level for manufacturing grade milk. If the average price paid producers for manufacturing grade milk is consistently below the announced support price when markets are at support levels, this is prima facie evidence that either the make allowance is too low or that competition is just not effective in getting money back to producers. During recent years at times when product markets have been at CCC buying price levels the manufacturing milk price has regularly been 40 to 55 cents under the announced price support level. Because of the size of the overall surplus this matter has not received the attention it deserves.

The manufacturing margins provided under the support program have not been increased since October 1, 1980. Although manufacturing plants until 1984 experienced certain efficiencies due to higher volumes, the savings in unit cost were not enough to offset the additional costs in labor, packaging and energy that those plants experienced. During the past year with a reduction in milk available for processing, many of the efficiencies have been lost and input costs have continued to increase.

The Federation surveyed its members' plants for December, 1984 to determine how much costs had increased since margins were last increased more than five years ago. The results of our study (Exhibit 4) clearly demonstrate the substantial increases in costs which have occurred in the major items used in the production of butter, nonfat dry milk and cheese. The data were submitted from plants located in all major production regions and all of the plants have experienced substantial cost increases in the cost items surveyed.

The survey also requested information on the cost of processing one hundred pounds of milk into cheese or into butter-nonfat dry milk. The survey indicated that the average cost of processing one hundred pounds of milk into cheese has increased 30 percent since 1979. A similar comparison for milk processed into butter-nonfat dry milk shows that those manufacturing plants had experienced a per unit increase of 45 percent. The slower rate of cost increase in cheese processing is due to fast changing technology in cheese making as well as to the fact that during 1984, the efficiencies in cheese plants were maintained by drawing milk from butter-nonfat dry milk plants. As a result, these latter plants experienced major cost increases per unit during the year. In light of the findings presented in the attached Exhibit 4 and the unit cost information supplied by our members, there is no doubt that the current margin structure is insufficient for plants of average efficiency to pay dairy farmers the support price when product prices are resting on supports. The manufacturing margins for cheese should be increased at least

$.30 per hundredweight, and that for butter and nonfat dry milk should be increased $.40 per hundredweight.

This should be done even if it requires some internal adjustment in the level of support so as to in effect retain the same level of purchase prices even though the dollars and cents price support level is lower. A price support level which is never achieved soon becomes meaningless.

An important index of milk values in the country is the Minnesota-Wisconsin price. The M-W price is used as the basis for establishing prices under Federal milk orders. About 70 percent of all milk marketed is regulated under the terms of Federal Milk Orders. A key question is,"What impact will a particular action have upon the M-W price?" My estimate is that the April 1 price support action which was intended to result in a 50 cent decrease in price support levels, will result in a 70 cent reduction in the M-W price from March to June.

(Attachments follow:)

Exhibit 1. Impact of April 1, 1985 Dairy Price Support Reductions on Value of 100 Pounds of Milk Manufactured into Butter and Nonfat Dry Milk

	Pre April 1		Post April 1	
	Chicago (dollars)	New York (dollars)	Chicago (dollars)	New York (dollars)
Purchase Prices				
Nonfat dry milk (nonfortified)	.9100	.9100	.8475	.8475
Nonfat dry milk (fortified)	.9225	.9225	.8575	.8575
Butter	1.4325	1.4625	1.4325	1.4325
Yields				
Nonfat dry milk 8.13 lbs.				
Butter 4.48 lbs.				
Gross return on nonfortified nonfat dry milk 1/	7.40	7.40	6.89	6.89
Gross return on fortified nonfat dry milk 1/	7.50	7.50	6.97	6.97
Gross return on butter 1/	6.42	6.55	6.42	6.42
Gross return on butter and nonfortified nonfat dry milk	13.82	13.95	13.31	13.31
Gross return on butter and fortified nonfat dry milk	13.92	14.05	13.39	13.39
Value of milk used in butter and nonfortified nonfat dry milk 2/	12.60	12.73	12.09	12.09
Value of milk used in butter and fortified nonfat dry milk 2/	12.70	12.83	12.17	12.17
Reduction due to April 1 Action:				
Butter and nonfortified nonfat dry milk	--	--	.51 3/	.64 3/
Butter and fortified nonfat dry milk	--	--	.53 3/	.66 3/

1/ Product price times yield.

2/ Gross return minus make allowance.

3/ If the impact of lower nonfat dry milk prices on dry butter milk returns is considered, the reduction would be three cents (.03) greater.

Exhibit 2. Impact of April, 1985 Dairy Price Support Reduction on the Value of 100 Pounds of Milk Utilized in Barrel and Block Cheddar Cheese

	Pre April 1		Post April 1	
	Barrel (dollars)	Block (dollars)	Barrel (dollars)	Block (dollars)
Purchase Prices Cheddar Cheese	1.3175	1.3475	1.2450	1.2875
Cheddar Cheese Yield: 10.1 lbs.				
Gross return on milk used in cheese 1/	13.31	13.61	12.57	13.00
Value of milk utilized in cheese 2/	11.94	12.24	11.20	11.63
By-product Credit:				
Fat	.36	.36	.36	.36
Whey solids	--	--	.10	.10
Milk value utilized in cheese plus by-product value	12.30	12.60	11.66	12.09
Milk value utilized in cheese plus fat credit but less whey by-product credit	12.30	12.60	11.56	11.99
Reduction Due to April 1 Action:				
If whey credit is recovered	--	--	.64	.51
If whey credit is not recovered	--	--	.74	.61

1/ Purchase price times yield.

2/ Gross return minus make allowance.

Exhibit 3.

National Milk Producers Federation
1840 Wilson Blvd., Arlington, VA 22201
703-243-6111

James C. Barr, CAE
Chief Executive Officer

May 17, 1985

The Honorable John R. Block
Secretary
U.S. Department of Agriculture
Washington, D.C. 20250

Dear Mr. Secretary;

At our May 10 meeting, the National Milk Producers Federation Board of Directors approved a resolution urging that you refrain from implementing a milk price support reduction of $.50 per hundredweight should USDA project that government dairy product purchases may exceed five billion pounds milk eqivalent during July 1985 through June 1986.

The Board expressed concern over the harsh negative impact such a cut would have on dairy farmers and the dairy industry so soon after the $.50 per hundredweight price reduction you implemented effective April 1.

We urge you to maintain the support price at the current level of $12.10 per hundredweight through the remainder of the current fiscal year, while dairy farmers work with you and the Congress in an attempt to formulate a workable dairy program for inclusion in the 1985 farm bill. Maintaining the support price at the present level would enable dairy farmers to adjust production levels to this new, lower price, while reducing the market instability caused by excessive price fluctuations.

Sincerely,

James C Barr

James C. Barr
Chief Executive Officer

JB/dl

Norman H. Barker President James P. Camerlo, Jr., First Vice President Herbert Selbrede, Second Vice President

Exhibit 4

Cost Increases in Production Items as Reported By NMPF Member Manufacturing Milk Plants

ITEM	December 1979	December 1984	Percentage Increase
	(dollars per unit)		
Energy			
Oil #2 per gallon (diesel)	0.8063	.9316	15.5
Oil #6 per gallon	0.4991	.7008	40.4
Gas per 100 cu. ft.	0.2947	.4788	62.5
Propane per gallon	0.4343	.5056	16.4
Electricity per kwh	0.0344	.0514	49.4
Labor Costs (including fringe benefits) per plant worker per hour	9.52	12.90	35.5
Packaging Costs			
per 50-lb. bag (NFDM approved for sale to CCC)	0.3948	.4765	20.7
per 68-lb. butter box (including liner and tape)	0.3248	.4108	26.5
per 40-lb. block cheese box (including liner and tape)	0.6056	.6922	14.3
per fiber drum for barrel (including liner)	4.9567	8.8567	78.7
Cleaning Compound			
liquid, per gallon	2.7056	2.1343	-21.1
dry, per pound	0.3578	.7834	118.9

March, 1985

FARMERS UNION
Milk Marketing Cooperative

S T A T E M E N T O F

FARMERS UNION MILK MARKETING COOPERATIVE
3225 East Washington Avenue
Madison, Wisconsin 53704

Presented by

James Eichstadt
Director of Communications

Before the

House Committee on Agriculture
Subcommittee on Livestock, Dairy and Poultry

1300 Longworth House Office Building
Washington, D.C. 20515

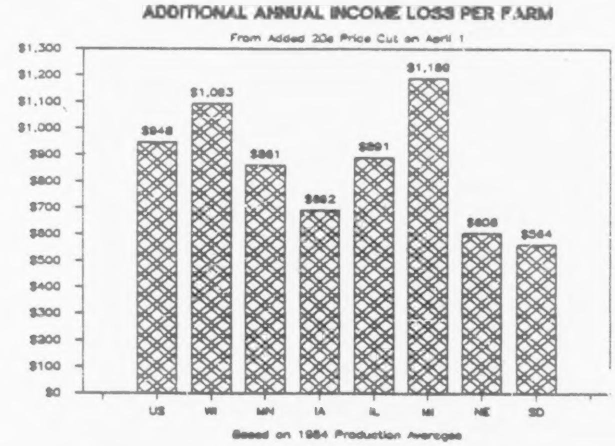
May 21, 1985

Mr. Chairman, I am James Eichstadt, director of communications for the Farmers Union Milk Marketing Cooperative based in Madison, Wisconsin. We represent more than 7,300 family dairy producers in the seven Midwest states of Wisconsin, Minnesota, Iowa, Illinois, Michigan, Nebraska and South Dakota. We thank you for calling this hearing on a subject so vital to the economic interests of our members.

We want to call attention to USDA's mishandling of the April 1 price support adjustment and its consistent failure in recent years to maintain farm milk prices at the levels mandated by Congress. If indeed the dairy program has failed in its basic mission, as critics charge, blame must be laid on the department's failure to administer the law, not on the dairy producers forced to survive under that law.

We strongly feel that the April 1 price cut implemented by Secretary of Agriculture John Block was excessive and outside of his authority. By our estimates, the new CCC dairy product purchase prices will reduce farm milk prices by 70 cents or more per hundredweight. The Dairy and Tobacco Adjustment Act of 1983 limited the Secretary's authority to reduce the support price to $12.10 per hundredweight on April 1, 1985 if projected annual CCC purchases exceeded 6 billion pounds milk equivalent on that date. In light of the Secretary's refusal to even consider an extension of the Milk Diversion Program, no one was surprised that the trigger level was exceeded. Be that as it may, there is nothing in the law which permits the huge support reduction imposed upon us last month. The Secretary's actions are arbitrary, illegal and harmful to the dairy industry, particularly those producers in the Upper Midwest who depend heavily on the manufactured dairy product market for their income.

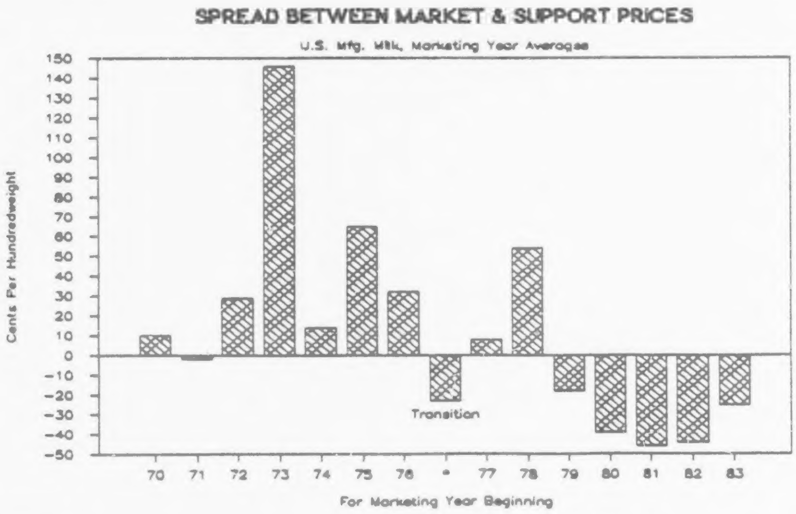
The average Wisconsin dairy producer will lose $1,093 in annual income as a result of the additional 20 cents per hundredweight taken by the April 1 support cut. Projected losses in other Midwest states include $1,189 in Michigan, $892 in Illinois, $861 in Minnesota, $692 in Iowa, $606 in Nebraska and $564 in South Dakota. This assumes that farm milk prices fall by 70 cents per hundredweight, or 20 cents more than they would were the law properly administered. The graph below depicts those average annual losses in our seven-state region and for the nation as a whole.



Mr. Chairman, the Subcommittee should do everything possible in the short time remaining to prevent the next scheduled price cut on July 1. We are already being penalized for much of the second price cut. Additionally, we fear that the department plans to repeat the excesses of April 1 with the next scheduled reduction. **The National Dairy News**, a respected industry trade publication, quoted a high-ranking USDA official in its April 12, 1985 issue as boasting, "I think we're going to do more of the same thing on July 1." This arrogance is totally inappropriate and indicates the Administration's disdain for the program.

Beyond our immediate concern with the April 1 cut looms a larger issue. USDA has consistently failed since the beginning of the 1979 marketing year to maintain farm milk prices at the minimum legal levels set by Congress. This period, coincidently, includes the Reagan Administration's entire term in office. We feel obligated to remind the department of its basic obligation under the law to maintain the average U.S. manufacturing milk price at the announced support level and hope that there is some legal remedy available to correct this sorry situation.

As the graph below illustrates, the average annual U.S. manufacturing grade milk price, which generally had been trending above the support level through the decade of the 1970s, fell below the support price in 1979 and has consistently stayed below that level since that time.



As shown in the graph below, monthly manufacturing milk prices have remained below the legal minimum during the period of 1980 to March 1985 with the exception of December 1983 and September 1984 to January 1985, when the effects of the Milk Diversion Program were being felt. This disparity between actual farm pay prices and the support level will continue to grow as the effects of the April 1 cut reverberate throughout the farm economy, accelerating the painful shakeout of some of the nation's finest, most efficient dairy producers and laying waste to our rural communities in the process.

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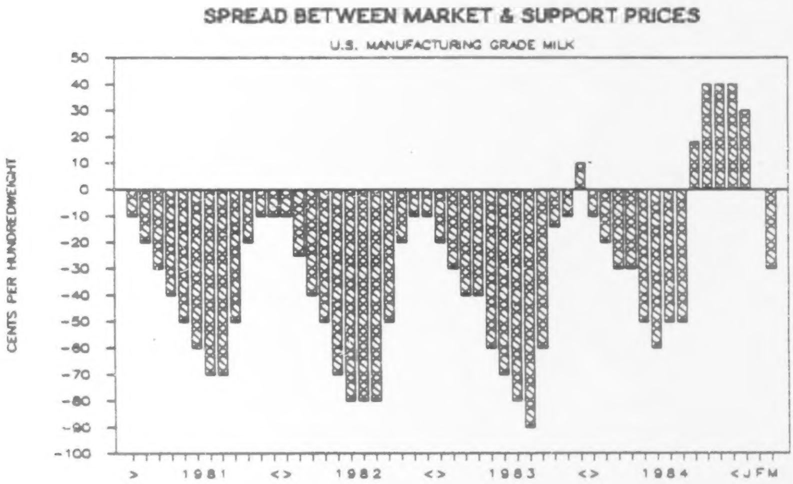

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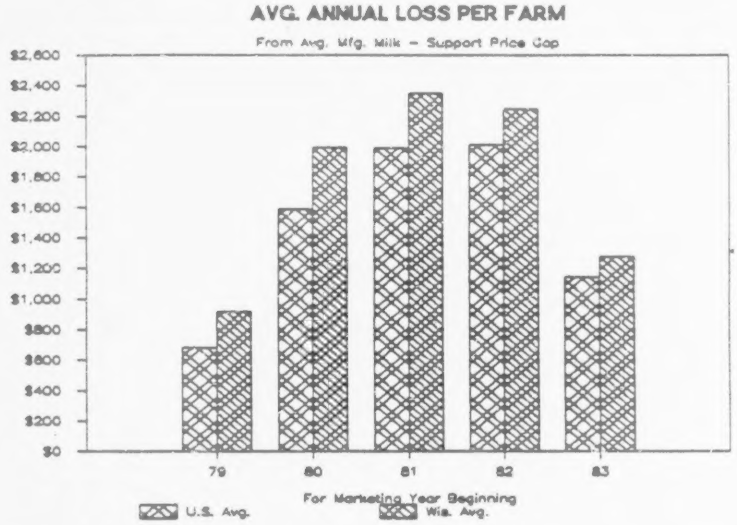
Dairy producers have been denied the fair milk prices to which they are legally entitled and generally assumed to be receiving. USDA's failure to maintain average manufacturing milk prices at the support level cost the average U.S. dairy producer $1,143 in lost income during the 1983-84 marketing year, with losses climbing as high as $2,009 in 1982-83. Since USDA counts all farms with milk cows, not just commercial operations, the averages understate the actual loss for the typical commercial producer. We estimated that the average Wisconsin producer, at 1,400 pounds of milk per day, lost as much as $2,351 during the 1981-82 marketing year, when the average manufacturing milk price was 46 cents per hundredweight below the support price.



Had the dairy program been properly administered, we may well not have the current surplus situation and the accompanying political pressures to dismantle a program which worked well from the time of its inception until the late 1970s. The lower prices received since the beginning of the 1979 marketing year have forced dairy farmers to produce ever more milk to meet the rapid rise in fixed operating expenses. We contend that the supply-demand imbalance would be much more manageable if producers had only received the additional income due them in recent years under the price support program. This deliberate policy of undercutting the price support program may make sense during the short term as a means to further the Administration's cheap food policy, but it is an extremely unwise agricultural policy which will prove harmful to the public interest over the long term as thousands of efficient dairymen are driven out of business.

On another basic issue, we challenge the assumption that the imbalance between milk supplies and demand can best be corrected through lower price supports. Research indicates that a 10 percent farm milk price reduction is needed to sell 2.35 percent more milk on the commercial market, meaning 1984 farm milk prices would have to drop 27 percent to move last year's 6.28 percent surplus production. The sharply lower prices which would result from further support reductions would only make the surplus worse as dairy farmers scrambled to recover lost income. Thus begins a vicious cycle of events in which more production begets lower prices, which in turn beget more production...ad infinitum, until even the most efficient operators are driven out of business. We hope Congress does not fall victim to the twisted logic of the price cutters and instead enacts a voluntary supply management program of the kind we recommended in previous testimony before this committee.

Again, Mr. Chairman and members of this committee, we appreciate this opportunity to speak out on the real problems facing the dairy price support program. Thank you.

STATEMENT BY TOM SAUNDERS
PRAIRIE FARM, WISC.

HOUSE COMMITTEE ON AGRICULTURE
LIVESTOCK, DAIRY AND POULTRY SUBCOMMITTEE

I am a dairy farmer from Prairie Farm in Barron County, Wisconsin, a member of the Wisconsin Farm Unity Alliance State Board and active in the Wisconsin Groundswell Coalition.

I would like to speak out strongly against the July 1st fifty cent price cut proposed by the administration. Rural economies throughout Wisconsin, are suffering from the effects of depression farm prices. A fifty cent price cut will directly cause the loss of millions of dollars of earned income to the Wisconsin economy, AS well as the nation. The result will be increasing farme foreclosures and small business failures.

Rural Wisconsin is in an economic crisis which can only be turned around by agricultural policies which provide long term stability and a return of fair prices for farmers, not irresponsible support price cuts. The Farm Policy Reform Act, Senate Bill 1083 and House Bill 2383, which calls for an increase in loan rates to 70% of parity, and mandatory supply management, if enacted, will do much toward returning stability to rural America.

Within the next several days, Senators Harkin and Zorinski in the Senate and Evans in the House will be introducing an amandment to the Farm Policy Reform Act which addresses dairy. This legislation, developed by the Wisconsin state NFO at the Dairy Committee of the Wisconsin Groundswell Coaltion is entirely consistant with SB 1083 and HR 2383 in that it calls for 70% support levels and mandatory supply management. This approach is fiscally conservative and market oriented, and the only real alternative to the surrent crisis.

In closing I would like to make one last comment. Through the next several months, many rural citizens and farmers will be coming to Washington to express their views as I am doing today. All of us in rural America have come to realize that for far too long we have left the political process up to elected officials and professional lobbyists. We intend to change this. I can assure you that we are serious about this effort. We realize that change will not happen overnight. We intend to work aggressively for the kind of reform that will provide economic justice for farmers and rural citizens, and the rest of the country as well. Thank you.

TESTIMONY ON DAIRY PRICE CUT

Hal Hamilton
Kentucky dairy farmer
Coordinator of Community Farm Alliance
Director of Henry County Farm Bureau, New Castle, Kentucky

I want to offer a dairy farmer's perspective on dairy policy and the proposed price cut. This perspective is not necessarily the perspective of the "dairy industry," but rather that of dairy farmers.

Dairy farmers currently face the following three problems of crisis proportions: insufficient income, surplus production, and a trend to concentration of production beyond optimal economies of scale. Legislation needs to be comprehensive and addressed to all three problems.

We all know the history of the problem: parity prices without supply management; tax break-subsidized productivity increases; and cheap grain, fueling the growth of feedlot dairies, especially in the Southwest.

Free market solutions are commonplace, and the July 1 cut is part of this mindless conventional "wisdom." We are told that lower prices mean lower production. On an individual farm basis, this is obviously false. When my income per cow drops, I add cows. In the aggregate, lowering price drastically enough does bankrupt farmers, of course, but is this the dairy policy we want?

It is time for our nation to make a decision about agriculture. We can choose what David Stockman calls a "dynamic economy," let the sharks eat the fishes, and eventually have a vertically integrated agriculture dominated by a few huge firms. Or we can choose an agriculture of family-scale farms sustained by federal intervention.

Federal intervention to guarantee family-scale production does not have to be expensive if we establish a system of quotas. Government purchase of surplus commodities benefits processors, but costs taxpayers and hurts farmers.

The support price system can work for a prosperous rural economy if 1) the price covers all production costs; and 2) quotas distribute production fairly, geographically and by farm size.

We need higher prices, not lower prices. And we need mandatory supply management targeted to family-scale farming. Farm policy should be constructed to serve farmers and should not be held hostage to those elements of the dairy industry that benefit from the flow of commodities into government storage.

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STATEMENT OF
THE SOUTHLAND CORPORATION
BY
DAVID A. BEREN

This statement is presented on behalf of The Southland Corporation. My name is David A. Beren. I am the economist for Southland's dairy operations.

Southland markets dairy products throughout the United States. Our 21 plants produce a full dairy line, including fluid milks, ice cream, cottage cheese, cream, eggnog, sour cream and yogurt. We service customers in all 50 states and the District of Columbia. We are also the world's largest operator and franchisor of convenience stores, with over 7,400 7-Eleven stores in the United States and 3,450 other retail units in Southland's International Division.

Drop Powder Supports And Leave Butter As Is

Placing the entire impact of the $0.50 milk support price drop on nonfat dry milk, rather than spliting it between powder and butter, moved the dairy industry toward greater market orientation and decreased government costs, without any negative impact on farmers. We urge the government to do this again on July 1.

The Southland Corporation believes the support program is essential to the dairy industry and fully endorses its continuation.

The best way out of the current surplus problem facing the dairy industry is to increase consumer demand. The industry at all levels is much healthier when we are competing for a large share of a growing pie, than fighting to survive in a shrinking market. For this reason a shining star of the 1983 Dairy and Tobacco Act was the creation of the national dairy advertising and promotion program.

With the key to a stronger industry lying in the demand factor, lets look in that direction to evaluate whether placing the entire April 1 support drop on nonfat drymilk was more advisable than splitting the drop between butter and powder.

The primary purpose of the support reduction was to move supply and demand closer together. During a large part of the last twelve months butter prices were based on actual market values, while milk powder continued to be supported above its real market worth. From June to early December 1984, butter prices were above the support level. Chicago Mercantile Exchange prices for Grade A butter were as high as $1.6075 a pound, 12% over the support level.

As for as butter was concerned the program operated as it was intended. That is, for six months fat pricing was based on market values and then when due to historically flush fat availability, which occurs in the winter when ice cream sales are low and fluid milk sales high, the support program undergridded the fat market. Thus providing the support it is intended to provide.

Looking at nonfat dry milk we see a very different story. During the entire period since January 1984 powder prices rested on support. The average price of nonfortified low heat powder stayed within $0.01 of the $0.91 support price.

Government purchases of milk powder never ceased even while a tremendous shortage of milk existed in many markets. At times when we had to haul milk over 600 miles to meet consumer demand for dairy products in some Texas markets, and milk had to be hauled all the way acorss the country from Wisconsin to Florida, some organizations continued to sell nonfat dry milk to Uncle Sam. Throughout this period of shortage the government purchased no butter.

Surplus Powder Far Outweighs Surplus Butter

The government inventory of nonfat dry milk greatly exceeds that of butter. On the average 100 pounds of cow's milk will produce 8.13 pounds of nonfat dry milk and 4.48 pounds of butter, a ratio of 1.8 to 1. However government inventories of powder excess butter by more than 6 to 1.

The Commodity Credit Corporation (CCC) currently has in stock 971 million pounds of uncommitted powder and 154 million pounds of butter. In other words, the surplus of powder is 3 times greater than the butter surplus on a milk equivalent basis.

We urge the U.S. Department of Agriculture to again in July take the entire reduction on nonfat dry milk and leave butter unchanged. Even with lower powder support prices and stable butter supports, again in 1985 as in 1984, we expect the commercial demand for fat from July through November to lift butter prices above the support level. When this occurs government butter purchases will cease. However, even at the reduced support level for nonfat dry milk it is unlikely powder demand will be sufficient to raise its price above the floor level.

What if this prediction is wrong and the lower nonfat dry milk price is below the market clearing level? If this were to occur it would not be a problem because powder prices would move above the support level, government purchases would cease, and the program would be functioning as it is intended to; one of supporting prices during the natural flush period and letting the market function during the short supply season.

Dropping Powder And Not Butter Decreases Program Costs

The CCC buys proportionately more nonfat dry milk than butter. Therefore, lowering powder supports only and leaving butter unchanged, decreases the cost of the support program.

Based on the amount of powder and butter purchased in FY84 (Oct. 83 - Sep. 84) the April 1 and July 1 cuts being entirely on nonfat dry milk would save the government about $20 million a year.

Dairyfarmer's Returns Not Affected By Butter Versus Powder Issue

Total returns to the nation's dairy farmers is not affected by how the government divides the support price reduction because their product, raw milk, is made up of both skim milk which produces nonfat powder, and milkfat from which butter is derived. In other words, what we are discussing is a method of reducing the cost of the dairy support program without decreasing dairymen's income.

In conclusion, we commend the government for its decision to take the entire April 1985 support price reduction off the nonfat dry milk price and urge it to do the same in July. All the reasons that made it a proper decision last month still exist today.

STATEMENT

OF THE

CHOCOLATE MANUFACTURERS ASSOCIATION OF THE U.S.A.

Richard T. O'Connell
President

Mr. Chairman, Members of the Committee, I am Richard T. O'Connell, President of the Chocolate Manufacturers Association of the U.S.A. (CMA). CMA represents fifteen companies who manufacture most of the chocolate and chocolate products produced in the U.S. These products include baking chocolate, chocolate confections, chocolate syrups and cocoa for drinking purposes, and chocolate-flavored milk. Our members also manufacture chocolate and cocoa ingredients used in ice cream, bakery goods, cereals, biscuit and cracker products.

The chocolate industry uses about $430,000,000 worth of milk annually, principally in the manufacture of milk chocolate. Milk chocolate constitutes about 90 percent of total chocolate confectionery sales. About 20 percent of a chocolate bar is milk.

The Chocolate Manufacturers Association supported the April 1, 1985 reduction in the dairy support price. We also support the July 1, 1985 scheduled reduction of another $.50 per hundred weight (cwt.).

CMA testified earlier this year in favor of the most simple and economically rational proposal to reduce dairy product surpluses and government costs. And that is, simply lower the price support. A lower price will decrease production, decrease government purchases and costs, and decrease the retail price of the product.

There is no other program change which can fairly treat the interests of the producer, the consumer, the taxpayer and the user.

The Dairy Diversion program, authorized by the Dairy Stabilization Act of 1983, where dairy farmers were paid not to produce milk, did not serve its intended purpose to reduce milk output and thus reduce surpluses.

Participation in the program was low and April 1985 statistics show April output at 12.0 billion pounds, up 3% from a year ago. Cow numbers were up nearly 1 percent from a year earlier with production per cow up 2 percent from a year earlier.

These figures prove that the Dairy Stabilization Act, with the diversion program as its main feature, has not improved longer-term prospects for balanced supply and use. Even with the July 1 reduction, we predict a 10.9 billion pound purchase of dairy products by the Commodity Credit Corporation.

The present dairy herd is not heavily culled and is relatively young with superior production capacity. If milk production incentives -- price support levels -- are not reduced, surplus production and enormous program costs can be expected to continue.

Another problem with a paid dairy diversion program is that it causes regional distortions in supply and demand as farmers in some regions sign up for the diversion program in greater numbers than others. This is of great concern to CMA members who buy dairy products in several regions of the U.S.

Mr. Chairman, paid diversion programs are economically artificial devices designed to hold milk support prices higher than demand suggests. A diversion program pays certain farmers in some regions not to produce milk while providing virtually no benefit to other producers, consumers, taxpayers and users.

Only by lowering price supports will supply be brought closer to demand and will the interests of all concerned be justly served.

Thank you.

NATIONAL
INDEPENDENT
DAIRY-FOODS
ASSOCIATION
SINCE 1957

321 D STREET, N.E. WASHINGTON, DC 20002 (202) 543-3838

NATIONAL INDEPENDENT DAIRY-FOODS ASSOCIATION

TESTIMONY

BY
DONALD A. RANDALL

BEFORE THE
HOUSE AGRICULTURAL COMMITTEE
MAY 21, 1985

Mr. Chairman, the members of the National Independent Dairy-Foods Association (NIDA) express their appreciation for this opportunity to assist the subcommittee on the issues raised by the April 1st support price reduction and the probable reduction for July 1, 1985.

NIDA agrees with both support price reductions for the reasons that they are needed by the industry as adjustments to induce lower milk production. An equally important reason for these reductions is the fact that they are the vital second step of the legislative program enacted in 1983.

Let us examine the reason for these two reductions. It seems clear that many in Congress in 1983 did not believe that the price reductions would occur in 1985 because the diversion program was their planned, accepted and "workable" method by which excessive milk production would be permanently reduced. The diversion program had a temporary, minimal impact, and the 1985 law should not contain even a standby diversion scheme. Since the

A merger of National Independent Dairies Association and National Association For Milk Marketing Reform

diversion program was a failure as a permanent surplus milk reducer, the safeguards enacted into the law (the two step price reductions) have automatically become effective.

Whether or not Congress made a mistake with the diversion program isn't the real issue here. Congress did not make a mistake on the price redutions, and neither did Congress make a mistake in granting the authority to the Secretary to estimate, plan and execute the price cuts.

NIDA agrees, on behalf of our cheese producers, that the CCC purchase price method for surplus cheese was actually in excess of 50¢ per cwt. of the fluid milk utilized. Some say perhaps 70¢ per cwt., but this is not the real problem in the industry. Everyone agrees that the real problem is the excessive purchasing by CCC of the mountainous quantities of surplus milk and its products. However, the interruptions in the markets by two successive price reductions following within 90 days might have been handled differently, but these inconveniences are unavoidable. It is arguable that the Secretary should not have placed the impact of the April 1st reduction on nonfat dry milk, but anyone who realistically looks at the commercial markets and recognizes who buys and disposes of nonfact dry milk, knows the reason. CCC creates the market and buys most of the nonfact dry milk.

Everyone we know of in our industry, who looks upon dairying as a profit making business, and not some social program of the federal and state governments, agrees that support price cuts are inevitable and necessary. We all know that we cannot spend our dairy farmers or their cooperative plants into prosperity, anymore than we could spend our handlers and their processing plants into prosperity. We have only pushed our farmers further from the real world of producing and selling in real markets to consumers who demand a quality product and use it.

The price reductions may be temporarily disruptive for some, but they are necessary, and the Secretary must use the most effective means at his disposal to achieve the end results. Anything less is probably a dereliction of duty.

We have attached a copy of the USDA's Dairy Market News, Vol 52, Report 14, dated April 1 - 5, 1985. It tells the story. CCC net removals with the two price cuts of 1985 will total 9.1 billion pounds of milk during the fiscal year. Net CCC outlays are $1,941,000,000. The figures speak for themselves.

Respectfully submitted,

Donald A. Randall

Donald A. Randall
Executive Vice President/
General Counsel

(Attachment follows:)

The Final Regulatory Impact Analysis for the support program for milk, 1984-85 marketing year (see announcement in last week's "Dairy Market News" (DMN) report, Volume 52, No. 13, pages unnumbered and Editor's Note below) considered two alternative support levels: (1) lower support price 50 cents per cwt. on April 1 to $12.10 per cwt. for milk containing 3.67 percent milkfat (selected) and (2) leave support price unchanged on April 1 at $12.60 per cwt. Several administrative changes also were made to the program: (1) Increase the price differential between block and barrel cheese purchase price from three cents per pound to 4.25 cents. (2) Establish a single, nationwide purchase price for butter. Heretofore, CCC announced only one purchase price for butter--at New York City. Prices at other locations were adjusted lower but could not be less than the New York price minus three cents per pound. (3) In calculating the new purchase prices for butter and nonfat dry milk (NDM), the decrease in the support price for milk used in making these products was allocated totally to NDM. (4) In calculating cheese purchase prices, the whey allowance value was increased from zero to a net return of 2.5 cents per pound of whey S.N.F. (5) The maximum acceptable moisture levels for cheese purchases by CCC was retained at 36.5 percent for barrels and 38.5 percent for blocks. A minimum moisture level for block and barrel cheese of 34 percent was established, below which CCC will pay no additional premiums. Manufacturing margins were unchanged at $1.22 per cwt. of milk for butter/NDM and $1.37 per cwt. of milk for cheese. Also, CCC sell-back policy remained unchanged with prices at 110 perent of the new support purchase prices. The expected impacts of the alternative support levels are shown in the following table which was included in the Impact Statement.

A copy of the Final Regulatory Impact Analysis can be obtained from Charles N. Shaw, U.S. Department of Agriculture, ASCS, P. O. Box 2415, Washington, DC 20013. Phone: (202) 447-7601.

MILK PRODUCTION, UTILIZATION, AND CCC REMOVALS

ITEM	UNIT	1982-83 1/	1983-84 2/	1984-85 3/	1984-85 4/
Support level	Per cwt.	$13.10	$13.10/$12.60	$12.60/$12.10/$11.60	$12.60
Deduction	Per cwt.	$.50/$1.00	$ 1.00/$.50	$.50/0	$.50/0
Milk Production	Bil. lb.	138.8	136.8	137.0	137.6
Farm use	Bil. lb.	2.4	3.2	3.4	3.4
Marketings	Bil. lb.	136.4	133.6	133.6	134.2
Beginning commercial stocks	Bil. lb.	4.6	5.2	5.2	5.2
Imports	Bil. lb.	2.7	2.8	2.8	2.8
Commercial supply	Bil. lb.	143.6	141.5	141.6	142.2
Commercial use	Bil. lb.	121.9	126.0	127.1	126.6
Ending commercial stocks	Bil. lb.	5.2	5.2	5.4	5.4
Total Utilization	Bil. lb.	127.0	131.2	132.5	132.0
CCC net removals	Bil. lb.	16.6	10.4	9.1	10.2
Butter	Mil. lb.	410	239	210	240
Cheese	Mil. lb.	820	540	475	525
Nonfat dry milk	Mil. lb.	1,047	768	720	780
Evaporated milk	Mil. lb.	22	24	25	25
Estimated CCC purchase costs	Millions	$2,716	$1,983	$1,556	$1,761
Net outlays 5/	Millions	$2,782	$2,000	$1,666	$1,871
Industry Deduction	Millions	$254	$833	$327	$327
Diversion Payments	Millions	---	$335	$602	$602
Net CCC outlays 6/	Millions	$2,528	$1,502	$1,941	$2,146
Number of cows	Thousands	11,075	10,918	10,840	10,885
Milk per cow	Pounds	12,529	12,532	12,640	12,640
Prices Received by Farmers:					
Manufacturing grade	Per cwt.	$12.66	$12.41	$12.13	$12.50
All milk sold to plants	Per cwt.	$13.58	$13.34	$13.20	$13.57
Effective price 7/	Per cwt.	$13.30	$12.72	$12.80	$13.17
Farm cash receipts 8/	Millions	$18,410	$17,460	$18,040	$18,620
Margin	Per cwt.	$13.99	$14.48	$13.07	$15.07
Retail value	Per cwt.	$27.56	$27.82	$28.27	$28.64
Retail cost	Millions	$33,600	$35,050	$35,930	$36,260

1/ $13.10 support, April 16, 1983, initial deduction and September 1, 1983 additional 50-cent deduction implemented. 2/ Two 50-cent deductions effective October and November 1983, followed by one 50-cent deduction effective December 1, 1983; $12.60 effective December 1, 1983. 3/ Projected; assuming 50-cent deduction through March 31, 1985, followed by $12.10 support price April 1, 1985, and $11.60 support price effective July 1, 1985. 4/ Projected; assuming 50-cent deduction through March 31, 1985 with $12.60 support price retained throughout the marketing year. 5/ Before deductions from and/or diversion payments to producers. 6/ After deductions and/or diversion payments. 7/ Price received by farmers after applicable deductions. 8/ Receipts adjusted to reflect deductions and/or diversion payments.

EDITOR'S NOTE: Corrections to DMN, Volume 52, No. 13—"Calculation of CCC Purchase Prices for Dairy Products with Support at $12.60 and $12.10 per cwt." (1) Support price for manufacturing milk, $/cwt. at 3.5% milkfat: effective 12/1/83-3/31/85, $12.31; effective 4/1/85, $11.81. (2) Butterfat differential: effective 4/1/85, 17.2 (cents).

SOURCE: Agricultural, Stabilization, and Conservation Service.

STATEMENT
OF THE
MILK INDUSTRY FOUNDATION
AND
INTERNATIONAL ASSOCIATION OF ICE CREAM MANUFACTURERS
PRESENTED TO
THE
SUBCOMMITTEE ON LIVESTOCK, DAIRY AND POULTRY
OF THE
UNITED STATES HOUSE OF REPRESENTATIVES

MAY 21, 1985

888 16th Street, NW
Washington, DC 20006
Telephone: (202) 296-4250

E. Linwood Tipton
Executive Vice President

I am E. Linwood Tipton, Executive Vice President of the Milk Industry Foundation and the International Association of Ice Cream Manufacturers, on whose behalf I am appearing today.

The Milk Industry Foundation (MIF) is the national trade association for dairy product processors--ranging in size from single plant operations to multi-plant corporations with a myriad of interests. Member companies represent over 80 percent of the domestic processing industry. MIF member companies number nearly 300, and are located in all 50 states and over 20 foreign countries. U.S. members operate over 1,000 plants, which process 85 percent of domestically consumed fluid milk and fluid milk products.

The International Association of Ice Cream Manufacturers (IAICM) is the trade association for manufacturers and distributors of ice cream and other frozen dessert products. IAICM's 320 members operate over 1,110 plants and distribution centers nationwide, and manufacture approximately 85 percent of the ice cream consumed in the U.S.

The members of both associations use about two-thirds of all the milk used in the U.S. to process the milk and ice cream products they produce.

We were most pleased with the April 1st reduction in the support prices and only regret that it was not done sooner. Mr. Chairman, you and other members of the Committee are well aware of the position of milk processors and ice cream manufacturers which urges rebalancing supply with demand through decreases in the price support level.

None of the make shift programs tried in recent years, i.e. assessments or paid diversions, are as effective, fair and equitable to all interests as are price reductions.

Assessments hold prices to processors, users, retailers and ultimately consumers higher than they should be in order to provide money for dairy farmers to pay the assessment. In reality it is a hidden tax on consumers of milk and milk products.

The actual price to dairy farmers would be the same whether the price is held high and an assessment is imposed or whether the price support level is directly reduced. However, because with an assessment consumers pay the higher milk prices, and the money is then given to the government in the form of an assessment, it must be regarded as a "consumer milk tax." This we oppose.

Paid diversion programs are also merely a device to hold milk support prices higher than they need to be and then pay certain farmers to reduce their production. This is particularly burdensome when combined with an assessment to pay its cost. Just think of it--you keep consumer prices high--then impose a "consumer milk tax" to pay the cost of countermanding the economic impact of keeping support prices too high.

Additionally a paid dairy diversion program grossly distorts the economics of supply and demand. Clearly last year's program created severe short term regional shortages while the CCC still purchased over 10 billion pounds of dairy products.

Paying dairy farmers to not produce milk, while keeping milk support prices high, and taxing consumers to provide the money for reducing the government CCC cost is not a dairy policy--it's a "makeshift" plan which avoids implementing a policy that will work for everyone, i.e. reducing milk support prices--thereby increasing consumption and decreasing production.

The adjustments to the dairy farmer sector will occur over a reasonable period of time and with minimal hardship given appropriate signals such as the April 1 price support reduction. It will not be distorted by artificial, non-market-oriented policies.

Mr. Chairman, we are quite,supportive of the action taken by the Administration to realign butterfat and non-fat solids values when it reduced the milk support price by .50 cents per hundredweight on April 1st. CCC acquisitions of nonfat dry milk have been exorbitant. Last year the CCC bought 20.6% of the nations butter production, 19.4% of our cheese production, and a phenomenal 59.4% of the nations production of nonfat dry milk.

For years, changes in milk support prices have been divided equally between butter and nonfat dry milk. This has gradually changed the ratio between nonfat solids prices and butterfat prices.

In 1954-55, when the government first began to buy nonfat powder in 100 pound bags, the relative prices were 15.15 cents per pound for powder and 58.7 cents for butter. This is a ratio of butter prices being 3.88 times powder prices. The most recent prices are .91 cents for powder and $1.46 for butter. Butter purchase prices are now only 1.6 times powder prices. The ratio has been changed drastically over the years.

In order to stop any further distortion or changes in the relationship, future downward changes would have to be allocated 2/3 to powder and 1/3 to butter. This would be a neutral change. This might well deserve consideration of the Administration for the July 1st change.

Mr. Chairman, we appreciate the opportunity to appear before you today. Thank you.

STATEMENT

by

The Trade Association of Proprietary Plants

Robert J. Williams, Executive Director

At May 21st Hearing on Price Supports

In regard to the April 1,1985 Price Announcement T.A.P.P. disagrees with the following:

1. Assigning a whey return value of 10¢/cwt. for average test milk, the effect is to reduce the price support level 60¢/cwt. instead of the Congressional mandated 50¢/cwt. Such a value was unwarranted. A relatively few plants realize any such value from whey. In fact whey represents a disposal cost for most cheese plants except for a relatively few large plants.
2. The manufacturing allowance of $1.37 and $1.32 for butter-powder and cheese milk respectively should be increased 10-15¢/cwt. In spite of increasing costs to manufacture butter-powder or cheese these manufacturing allowances haven't been increased since 1981. The effect of understating these costs in the price support calculation is to make it impossible to return the full objective price support level to producers.
3. By assigning a 10¢/cwt. whey value and not up-dating manufacturing costs in the price support formula it will be impossible to reach the objective price support level of $12.10/cwt. On April

   1st the Department should have reduced the consumer price 3-4¢ instead of 6-7.25¢/lb. of cheddar cheese. This would have allowed for an increase in manufacturing allowance and negated the 10¢/cwt. unrealistic whey value. It would have fulfilled the Department's responsibility in decreasing producer prices 50¢ under the April 1 price support announcement.
   Using an understated , unrealistic manufacturing allowance made the price support obsolete to start with. Adding an unrealistic whey value compounds the inaccuracy of the price support formula. Both inaccuracies result in a lower price for producers and a lower price of dairy products for consumers, with the price for producer milk lower than was intended by Congress.

In regard to the July 1 legislated price support drop: The Department should make proper calculations as suggested above to bring the objective price support level into the actual levels mandated by Congress.

Consideration should also be given to hold the price support level at a realistic $12.10 level and re-institute a 50¢ producer assessment beginning July 1,1985 as a stop gap measure before the 1985 Farm Bill is passed.

Three factors should be considered in establishing any price support level, namely: Government costs, Farmer income and Consumer price.
Government costs should be the primary consideration in a time of budget deficits. In the time between July 1 and Oct. when a new dairy program is developed, one can expect heavy Government purchases and costs. A 50¢ assessment would substantially reduce Government costs.

The $12.10 price support minus a 50¢ assessment would net farmers a $11.60 price support level which should give farmers the proper price signal. It is the same level as the scheduled level under present legislation.

The effect of the $12.10 price support level would be to freeze consumer prices 50¢ over the intended July 1 price levels. In effect, this freeze would help solve the Government cost problem indirectly through through the farmer paid 50¢ assessment. Dairy products by any measure already are an excellent buy. A further decrease in consumer prices is unwarranted.

If prospects are good that the new Farm Bill in Oct. will contain an assessment and diversion program, the price support would have to be raised to $12.10 or higher coupled with a 50¢ assessment to net farmers $11.60/cwt. minimum. Lowering consumer price in July and then raising it again in Oct. would be unwise from a political and practical standpoint.
Longer term stability of price in the long run would be beneficial to both consumers and producers.

So temporary legislation should be considered between July 1 and Oct. 1 to maintain the $12.10 price support level to consumers and reinstitute a 50¢ producer assessment. This will give producers the proper price signal, stabilize consumer prices and reduce Government costs substantially. It would also provide a smooth transition from the present program to a new program Oct. 1,1985.

Your consideration of these matters would be greatly appreciated and would be in the long term best interests of farmers, consumers and tax payers.

Thank you.

Robert J Williams